# BURGESS' COMMERCIAL LAW

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# BURGESS' COMMERCIAL LAW

A TEXT BOOK FOR ALL CLASSES OF SCHOOLS AND COLLEGES IN WHICH COURSES ARE OFFERED IN COMMERCIAL LAW

BY

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# PREFACE

Those who compose classes in commercial law are, as a rule, without business experience, in fact, without much of any sort of experience in life. The subject consists almost wholly of a study of business situations and relations that have been unthought of by the pupil. Given a certain state of facts; the law is a statement of the rights and obligations of the parties growing out therefrom. It is therefore of itself a generalization. To be comprehended the particulars on which it is founded must be clearly understood, for a knowledge of the particular in this case must precede a knowledge of the general.

The subject is therefore not an easy one to teach and the teacher needs every aid he can secure from his textbook. In the preparation of this book both the teacher and the pupil have been kept constantly in mind; classroom conditions have been ever before the authors. The experienced teacher comes to know where pupils have difficulty and what they comprehend without great effort. A knowledge of these matters has enabled the authors to give unusual attention to many topics in the text that have in the past given some trouble to teachers.

It has also been found that some very important matters of frequent occurrence in business have not heretofore been mentioned in any text. Such topics as the standing of the merchant's rule in case of partial payments; when a creditor is entitled to annual interest and when not; when title to goods passes in case of C.O.D. shipments, are but illustrations. These and many others like them are considered in this text in an authoritative manner.

It is believed that this text will be found to be well balanced, giving proper attention to each topic; and above all things the authors express their confidence in the superior teaching qualities of the book, fully believing that a textbook is valuable not so much for what it contains as for what the pupil may be able to get from it and make his own.

The time allotted to the study of Commercial Law varies widely in different schools. *Burgess' Commercial Law* is designed

to meet the needs of the average school in this respect. For schools that devote unusually short periods to the subject, or where the time allowed is unusually limited, the authors suggest the omission of chapters XXXI, XXXII, XLI, XLII, XLIII, and XLIV. It is believed that it will be much better to omit bodily the topics treated in these chapters than to attempt to shorten the course by hasty work throughout.

# CONTENTS


| CHAPTER | | PAGE |
|---|---|---|
| | **Contracts in General** | |
| I. | Kinds of Law | 1 |
| II. | Property | 7 |
| III. | Contracts | 11 |
| IV. | Competent Parties | 21 |
| V. | The Agreement | 30 |
| VI. | Consideration | 40 |
| VII. | Subject Matter | 47 |
| VIII. | Discharge of Contracts | 52 |
| IX. | Discharge of Contracts by Breach | 62 |
| X. | Remedies | 69 |
| XI. | Special Defenses | 74 |
| XII. | Miscellaneous Matters | 85 |
| | **Negotiable Instruments** | |
| XIII. | Negotiable Instruments | 93 |
| XIV. | Drafts | 104 |
| XV. | Checks | 112 |
| XVI. | Notes | 119 |
| XVII. | Holder in Due Course | 126 |
| XVIII. | Transfer | 135 |
| XIX. | Presentment for Acceptance | 144 |
| XX. | Presentment for Payment | 151 |
| XXI. | Interest | 160 |
| | **Guaranty and Suretyship** | |
| XXII. | Guaranty and Suretyship | 167 |
| | **Sales of Personal Property** | |
| XXIII. | Sales of Personal Property | 178 |
| XXIV. | Form of Contract of Sale | 184 |
| XXV. | Transfer of Title | 191 |
| XXVI. | Transfer by Bills of Lading and Warehouse Receipts | 200 |
| XXVII. | Warranties | 207 |
| XXVIII. | Remedies of Parties | 212 |
| | **Bailments** | |
| XXIX. | Bailments | 218 |
| XXX. | Bailment for Benefit of Bailee | 225 |
| XXXI. | Bailments for Mutual Benefit — Hire | 231 |
| XXXII. | Exceptional Bailments | 238 |

| CHAPTER | | PAGE |
|---|---|---|
| | **Agency** | |
| XXXIII. | Agency | 248 |
| XXXIV. | Agency—Duties of agent | 256 |
| XXXV. | Agency—Duties of principal | 262 |
| XXXVI. | Agency—Liabilities of third persons | 269 |
| | **Partnership** | |
| XXXVII. | Partnership | 275 |
| XXXVIII. | Partnership—Authority of partners | 282 |
| XXXIX. | Dissolution of Partnership | 288 |
| | **Corporations** | |
| XL. | Corporations | 296 |
| XLI. | Corporations, continued | 310 |
| | **Joint Stock Companies** | |
| XLII. | Joint Stock Companies | 318 |
| | **Insurance** | |
| XLIII. | Insurance | 320 |
| XLIV. | Insurance, continued | 329 |
| | **Real Estate** | |
| XLV. | Real Estate | 337 |
| XLVI. | Real Estate Conveyances—Deeds | 347 |
| XLVII. | Real Estate Conveyances—Mortgages | 358 |
| XLVIII. | Real Estate Conveyances—Leases | 367 |
| | Index | 375 |
| | Appendix | 381 |

# BIBLIOGRAPHY

It may at times be found advantageous to supplement the discussion in the text with reference books. The student may often obtain access to such books in a law office or law library. If these sources are not available, the following books are suggested as appropriate for reference. The publisher's name is shown in parenthesis following the name of the author. These books may be purchased through any standard law book dealer, and second hand copies may often be secured. One book on a subject will be found sufficient.

## CONTRACTS

| | Price |
|---|---|
| Harriman, E. A. (Little, Brown & Co., Boston, Mass.) | $3.00 |
| Clark, W. L. Jr. (West Publishing Co., St. Paul, Minn.) | 3.75 |

## NEGOTIABLE INSTRUMENTS

| | |
|---|---|
| Norton, Ed. by Moore & Wilkie (West Publishing Co., St. Paul, Minn.) | 3.75 |
| Bigelow, M. M. on Bills and Notes, (Little, Brown & Co., Boston, Mass.) | 3.00 |

## GUARANTY AND SURETYSHIP

| | |
|---|---|
| Spencer, E. W. (Callaghan & Co., Chicago, Ill.) | 4.00 |

## SALES

| | |
|---|---|
| Burdick, F. M. (Little, Brown & Co., Boston, Mass.) | 3.00 |

## BAILMENTS

| | |
|---|---|
| Goddard, E. C. "Outlines" (Callaghan & Co., Chicago, Ill.) | 2.50 |
| Schouler, J. (Little, Brown & Co., Boston, Mass.) | 3.00 |

## AGENCY

| | |
|---|---|
| Mechem, F. R. "Outlines" (Callaghan & Co., Chicago, Ill.) | 2.00 |
| Tiffany, F. B. (West Publishing Co., St. Paul, Minn.) | 3.75 |

## PARTNERSHIP

| | |
|---|---|
| Mechem, F. R. (Callaghan & Co., Chicago, Ill.) | 2.50 |
| Burdick, F. M. (Little, Brown & Co., Boston, Mass.) | 3.00 |

## CORPORATIONS

| | |
|---|---|
| Marshall, W. L. (Callaghan & Co., Chicago, Ill.) | 5.00 |

## REAL ESTATE

| | |
|---|---|
| Tiedeman, C. G. (F. H. Thomas & Co., St. Louis) | 6.00 |
| Goodwin, F. (Little, Brown & Co., Boston, Mass.) | 4.00 |

## LAW DICTIONARIES

| | |
|---|---|
| Anderson, W. C. (T. H. Flood & Co., Chicago, Ill.) | 5.00 |
| Cyclopedic Law Dictionary (Callaghan & Co., Chicago, Ill.) | 6.00 |

## GENERAL OUTLINE OF MUNICIPAL LAW

of which *Commercial Law* is a part

- I. Constitutional
  - 1. National
  - 2. State
- II. Statute
  - 1. National
    - a. Civil
    - b. Criminal
  - 2. State
    - a. Civil
    - b. Criminal
- III. Common
  - 1. Civil enforced by
    - a. Suits at law
    - b. Suits in equity
  - 2. Criminal

# BURGESS' COMMERCIAL LAW

## CHAPTER I

### KINDS OF LAW

**1. Law** is a rule of action or conduct, prescribed by an authority able to enforce its will.

Law is in its nature a command. The head of the family, who in the most ancient times regulated its encampments and employments, was among the first of "law-givers," and his directions, being the orders given by one who had power to enforce them, were the earliest "laws." If his laws were not observed he provided a suitable *penalty*, and his power to inflict the penalty gave him indirectly the power to enforce the law.

**2. The Object of Law** is to protect persons in the enjoyment of their rights and to punish others who interfere with these rights. The rules of action or conduct, of which law consists, define, limit, and protect the rights of the individual living in organized society.

A person of suitable age has a right to attend a public school, because the law declares that he may do so. His father has a right to vote for public officers, because the law has given him this right. Each person has thousands of these law-given rights. He has among other things, the right to life, the right to liberty, the right to marry, the right to acquire property, and the right to make contracts.

Each time that the law declares that one person may have certain rights by conforming to certain standards, it likewise declares that other persons must respect these rights. The object of law being therefore to define rights and to protect persons in their enjoyment of these rights, it is essential that our inquiry be directed in every instance, not only to determining what the law is, but to discovering the individual's rights and duties in respect to the law.

**3. Municipal Law*** is that body of rules which govern the conduct of the individual, prescribed by the supreme power in the state,† commanding that which is right and prohibiting that which is wrong. If the law-giving authority is the state, then the rule which it prescribes is termed "municipal" law. The word "municipal" is a survival of the language of ancient times when the city (municipality) was the supreme power, as were Athens and Rome. In modern times the term is applied also to laws prescribed by nations and independent states, as England, the United States, Illinois, or Texas.

That municipal law is necessary to the existence of a state, or other government, is seen when one realizes that without laws the state could not be kept together. It would be only an unorganized mass of individuals. In such unorganized society there would be present a tendency on the part of some individuals to be unjust to others. In order to protect itself, and to protect the individual, society must group itself into units, or states, with power to create and enforce municipal laws.

**4. Extent of Laws.** Each unit, which may be either a nation or the sub-division of a nation, must have its own laws governing the conduct and property of individuals within its boundaries. It follows that the laws created by a unit of society can be enforced only within its boundaries, and have no application to persons residing in other units, except when they come within its boundaries to reside or to transact business.

**5. Kinds of Municipal Law.** In our own country there are three kinds of municipal law, namely, (1) Constitutional Law, (2) Statute Law, and (3) Common Law. They are here stated in the order in which they have precedence when they conflict.

**6. Constitutional Law** is that body of laws which enumerates the rights and limitations of the government, the mode of

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* The terms "Natural" and "Moral" Law are frequently employed, but the use of the word "law" in such connection is with a meaning different from that in which it is used in this text. A discussion of International Law is also omitted from the text for the reason that its source, manner of enforcement and rules are of little value to the business man or to his correct understanding of the principles of commercial law.

† The term "State" must not be understood to be restricted to one of the political units of the United States, but to have that broader meaning that includes any political body of people who are united under one government, whatever the form of it may be.

exercising those rights, and the relation of the sovereign state to the citizen.

In the United States there is a divided sovereignty. When the original states met to form the Union, they voluntarily surrendered some of their rights to the Federal government, keeping the remainder to themselves. In the Federal constitution, which they formed, they enumerated the powers which the new Federal government should have, and strictly limited it to these specified powers. The powers and rights which were not expressly delegated to the Federal government in this Federal constitution were reserved to the states. Each state also has a constitution which represents the will of the people of the state, declaring and limiting the powers of the state toward its citizens.

**7. Statute Law** is that body of rules of conduct and action enacted by the legislative body of a state or nation, by virtue of the powers given in the constitution. These usually take the form of defining the rights and duties of persons toward each other and toward the state. When it is desired that new rights and duties should be defined and created, a bill is presented before the legislative body. If it is adopted by the legislative body and approved by the executive officer of the unit of government, the bill becomes a statute and is binding on all persons within the boundaries of the unit declaring it.

Thus if the Federal government desires to create a law regulating train service between two states, a bill to this effect may be passed by the U. S. Congress. When approved by the President the bill becomes a new Federal statute, which will then be binding on the railroads. Or if a state desires to regulate the sale of cigarettes within its boundaries, a bill to this effect may be passed by the state legislature. When approved by the governor the bill becomes a state statute, which will be binding on all persons within the state.

**8. Common Law.** Not all rights and duties as between individuals have been defined by either state or Federal statutes. When no statute exists so defining these rights and duties on a particular subject, a body of rules of conduct and action known as the *common law* applies. This common law is also called the *unwritten law*, because it is not *formally* expressed as is statute law. It is found in the reported decisions of the courts. It

came into existence at an early day when English courts were frequently called upon to decide disputes about matters which were not covered by statutes. The courts decided these matters on principles of justice, and when a similar case again came before the court, it decided this in the same way that the previous case had been decided. The policy was thus established of looking back to see how former disputes of a similar nature had been decided, and when a decision was found on a similar point it was called a *precedent*. The general body of the common law consists of these precedents.

The following will show how the different states adopted the English law.

"That the common law of England so far as the same is applicable and of a general nature, and all statutes or acts of the British parliament made in aid of, and to supply the defects of the common law, prior to the fourth year of James the First, and which are of a general nature and not local to that kingdom, shall be the rule of decision, and shall be considered as of full force until repealed by legislative authority."— Act of the General Convention of Delegates of the Colony of Virginia, held at Williamsburg, Monday, May 6, 1776.

Similar statutes have been passed by most if not all of the states except Louisiana, which being colonized by the French adopted the system of law in vogue in France, known as the *Civil Law*.*

**9. Order of Precedence.** The Federal constitution consists of an enumeration of certain rights and powers relinquished by the states to the general government; it is, therefore, the supreme law of the land in regard to all matters contained in it. The Federal statutes, being made in strict accordance with the constitution, must necessarily come next in order. The states, as we have seen, reserve to themselves supreme authority on many questions; they have also placed numerous restrictions upon their own government. In regard to all these matters the state constitutions of the several states are supreme in authority. State statutes made in accordance with the state constitution are next in authority. The common law applies when there is no constitutional law or statutory law which will apply. When there is a conflict between a statute and the common law, the statute takes precedence.

* The term *Civil Law* as employed in this connection is used only in the sense of distinguishing it from the *Common Law* of England.

Since the common law is in force wherever there is no statute upon a subject, it supplies what in many cases would be a great deficiency in our statute law. No legislature could possibly foresee and provide for all the possible contingencies and difficulties that could, and do, arise in the business relations of a complex civilization.

**10. Courts. Their Function.** Not only has organized society adopted a body of rules of action and conduct, but it has provided a means by which these rules can be enforced. The organized instrumentalities for interpreting and enforcing laws are called courts. A court has three functions. These are, (1) to decide in case of dispute what the law is, (2) to punish persons who violate the law, and (3) to compel one person to render justice to another.

Federal statutes are usually enforced by Federal courts only, which courts also decide matters arising under the Federal constitution, and disputes between citizens of different states. State courts enforce the state statutes, decide questions arising under the state constitution, and interpret and enforce the common law in cases that come under the jurisdiction of the state.

In the present text we shall study only questions of *civil* law as distinguished from *criminal* law. Criminal law defines, and provides penalties for, offenses against the state and society at large; civil law regulates the conduct of individuals towards each other. Both are often enforced by the same courts.

We shall treat of the courts as deciding the questions which may arise between business men, but the student must bear in mind that the courts of the present do not *make* the law — that is the function of the legislative branch of our government. Courts merely interpret and enforce the law.

**A suit at law** is the method by which a dispute over legal rights and duties is brought before the court. It is the method by which one person, who believes his rights to have been violated by another, may compel the latter to come before the court to have decision made in the matter. If it be decided that a right has been violated, the person who has been injured is given an appropriate remedy.

The term *suit at law* is sometimes used in a more restricted sense as distinguished from a *suit in equity*. The word *equity* means *justice*. Equity courts are special courts to which are

taken disputes in which substantial justice can not be secured under the statutes and precedents by which courts of law must be guided.

Today the chief distinctions between a suit at law and a suit in equity is that the former is usually tried by a jury, the latter by a judge; and that in the former money damages are usually the only remedy, while in the latter the remedy may be of a more personal nature, as compelling a man to do that which he promised to do, called remedy by *specific performance*, or prohibiting him from doing something unlawful which he threatens to do, called remedy by *injunction*.

Equity courts also deal with matters of divorce, mortgages and trusts. The distinction is of little practical importance to the business man except that he should understand the nature of the remedy which he may secure in the different courts. Some matters can be tried by a suit at law only; some by a suit in equity only; some by either as the person injured may elect.

**11. Commercial Law** is that part of municipal law applicable to business transactions. It is not an isolated branch of law, but includes a variety of topics whose only relation to each other is that they are all of importance in the transaction of the ordinary affairs of commerce.

It is the existence of law which differentiates civilized from barbaric society. Because of law the man of business dares to engage in ventures which may bring him no immediate return. He dares to acquire property, to place his money in the bank or to invest it in commercial undertakings, to agree to buy and to sell commodities in the future. Without law and law-defined rights he could not safely do any of these things. It is therefore of importance for every business man to know the municipal law in so far, at least, as it deals with the affairs of commerce.

## CHAPTER II

## PROPERTY

- I. Kinds
  - 1. Real
  - 2. Personal
    - a. Things in possession
    - b. Things in action
- II. As to time of enjoyment
  - 1. In possession
  - 2. In expectancy
- III. How held
  - 1. In Severalty
  - 2. In Joint Tenancy
  - 3. In Tenancy in Common
  - 4. By Partners
  - 5. By Corporations
  - 6. By Joint Stock Companies

**12. Property** in its legal sense is anything to which one has title. *A property right* is the power or dominion over a thing to the exclusion of others. Property is not, as commonly supposed, the thing itself, but is the right to the thing. By the ownership of property one is given the right to use, enjoy, and dispose of it, without any limitation except that it must not be used to the injury of another, or contrary to law. That one is possessed of a property right may be evidenced by actual physical control, or the evidence may consist merely of an *instrument of title*, that is, some legal document in writing, such as a warehouse receipt, a deed, a note, or a bill of lading. Actual possession is not necessary to establish a property right.

**13.** Property may be either *real* or *personal.*

**Real property,** *realty*, or *real estate*, includes all property which is fixed or immovable, such as land, together with what is permanently attached to it, or is built or growing upon its surface, and the minerals which are beneath the surface. Things

which are annexed to the soil or the building, with the intention that they shall become permanent improvements, or things which cannot be removed without injury to the soil or buildings, are also real property, and are called *fixtures*. Such are chimneys, pumps, fences, and the like.

There are three apparent exceptions to the rule that things annexed to the land become real property. These are where the thing so annexed is (1) a trade fixture, (2) a domestic fixture, or (3) an agricultural fixture. Such things are installed by the occupant for his own convenience while he occupies the premises. He may remove them at any time before he leaves. But if he surrenders possession of the land without removing them, even such things are considered to be real property and may be treated as such by the person to whom he has surrendered possession.

EXAMPLE

Josslyn rented a store of McCabe and put into the store shelving loosely attached to the walls, to hold dry-goods. When Josslyn moved to another store he left this shelving, intending to remove it later, but when he attempted to remove it McCabe refused to allow him to do so. In a suit at law, the court decided that McCabe was right, and that, although the shelves were trade fixtures and could have been removed by Josslyn so long as he had possession of the store, he lost his right to remove them when he surrendered possession and they were then to be treated as annexed permanently to the land and as real property. Josslyn vs. McCabe, 46 Wis. 591*.

**14. Personal property** is anything that is movable, that a person may take with him wherever he goes. The legal term "chattel" is often used to designate an article of personal property. Trees while growing upon the land are usually considered real estate, but when cut and lying as logs or lumber, they are personal property, or chattels. Similarly, minerals while yet in

* This is the uniform method adopted by all legal text-books in referring to a decision rendered by a supreme court of a state or nation. The first figure refers to the volume and the last to the page. In the above example this case will be found in volume 46 of the supreme court reports of the state of Wisconsin on page 591. Similarly, 91 U. S. 52, refers to volume 91 of the supreme court reports of the United States on page 52. The terms "N. W.", "N. E.", "Atl." etc., refer to a collected series of state reports in which the decisions of several states in a section of the country are bound together in one volume. For example, the N. W., or Northwestern reports, include the states of Iowa, Nebraska, Minnesota, North Dakota, South Dakota, Wisconsin, and Michigan.

the earth are a part of the realty, but when dug and thrown out on the ground they become personal property.

It is therefore evident that a thing which is personal property may become real property, by being permanently annexed to the land or buildings, and also that a part of the real estate may be severed and become personal property.

**15.** Personal property is divided into things in possession and things in action.

**Things in possession** are those things which the owner not only has the right to, but also actually possesses. All material objects, such as money, tools, garments, or vegetables and plants when not growing in the ground, and all domestic and tame animals, may be things in possession.

**Things in action** naturally include all those things to which one has merely a right, but not the actual possession. This name is given them because at the proper time the owner may, if he wishes, bring an action at law to give him possession of them. All forms of indebtedness, whether evidenced by notes or on account, are things in action.

EXAMPLE

1. If A has a thing in possession, as a horse, and sells it to B, taking B's written promise that at some future time he will pay $200 to A for the horse, B's obligation to pay, which is evidenced by the note, is a thing in action to A. When the debt is paid, the money is a thing in possession.

2. If Ames injures Bates by striking him wilfully, Bates has a right to recover all the damages which he suffered because of the injury from Ames. This right is also a thing in action, which may by a suit at law be reduced to a right in possession.

**16. Time of Enjoyment.** It is usual for the person who owns property to have also the right to its present enjoyment, that is, to use it at once if he so desires. There are some instances, however, in which the owner is considered as having a property right in the thing, but his enjoyment of it is postponed until some future time. In such a case his property right is said to be a right in expectancy. For instance, it often happens that a man wills his home to his wife to enjoy during her life-time, and after her death to his son. At the death of the husband both the wife and the son get property rights in the home, but the son's right to enjoy his property is postponed until the wife's death.

**17.** Property is held in *severalty* when it is all owned by a single individual.

It is held in *joint tenancy* when two or more persons take ownership of the same piece of property at the same time, with the same interest, and by the same written document, or instrument. These joint tenants each own an equal interest, not only in every part of it, but in the whole, and each is entitled to possession of the whole. Each receives an equal share of the proceeds of the property. The striking peculiarity of this way of holding property is what is called the *right of survivorship*; when one of the joint-tenants dies, the entire property belongs to the surviving joint-tenant or joint-tenants, until finally the last survivor is entitled to the whole estate. Both real and personal property may be held in joint tenancy, though a joint tenancy in personal property is extremely rare.

Joint tenancies were favored by the early common law, but are not now favored in the United States, and in many states* the right of survivorship has been abolished by special statute, in whole or in part. Other states require that unless the intention to create a joint tenancy is clearly expressed, the tenancy will be considered to be a tenancy in common.

Property is held in *tenancy in common* when two or more owners possess either equal or differing shares in it, without the right of survivorship. On the death of one such tenant in common, his share passes to his heirs, or personal representatives.

**18.** Property may also be owned by partnerships, corporations or joint stock companies.

* Arkansas, California, Iowa, Kansas, New York, Pennsylvania, South Carolina, Ohio, Connecticut, Kentucky, Mississippi, Colorado, and Tennessee.

## CHAPTER III

## CONTRACTS

- I. Essentials
  1. Competent Parties
  2. Mutual Agreement or Assent
  3. Consideration
  4. Legal Subject Matter
- II. Kinds as to Validity
  1. Valid
  2. Void
  3. Voidable
  4. Unenforceable
- III. Kinds as to Solemnity
  1. Formal, or Contracts under Seal
  2. Simple
     a. Written
     b. Oral
     c. Implied
- IV. Kinds as to Expression
  1. Express
  2. Implied
- V. Kinds as to Time of Performance
  1. Executory
  2. Executed
- VI. Relation to Each Other of Parties on Same Side
  1. Several
  2. Joint
  3. Joint and Several

**19. Introductory.** In the preceding chapter it was stated that one of the law-given rights of the individual was the right to make contracts. Without this right the transaction of present day business would be impossible. The right to make contracts is the basis of even the most minute of the individual's commercial activities. When he pays a nickel on entering a street car, when he orders groceries sent to his home, even when he buys a

newspaper on the street, he is exercising this right to make contracts. The contract is the instrument, the medium, by which modern business is transacted, and by its use one person may acquire a special control over the acts and property of others.

**20. A Contract** is an agreement between two or more competent parties, based upon a sufficient consideration, to do or not to do some lawful, possible thing. This definition contains four important essentials, or conditions necessary to create a contract, which are discussed in detail. These conditions are:

1. Competent parties,
2. Mutual agreement,
3. Consideration,* and,
4. Legal subject-matter.

For the present it will be necessary to consider a contract only from the standpoint of offer and acceptance, which together make up the mutual agreement. Every offer which is accepted does not become a contract, because the other conditions of the contract relation listed above may not be present. But every contract does consist in its essential parts of these two things — offer and acceptance. When Ames offers to sell his horse to Bates for $100, if Bates says, "I accept," then there comes into being a contract. Thereafter if Ames refuses to deliver the horse, Bates may sue him for the refusal; or if Ames has delivered the horse and Bates refuses to pay, then Ames may sue for the agreed price. At the outset we must conceive of every contract as consisting of these two elements.

**EXAMPLES**

1. Smith says to Jones, "If you will agree to dig my well, I will pay you fifty dollars for your work." Brown, who overhears this statement, says, "I will accept that offer." This does not create a contract, because Smith made no offer to Brown.

2. Baldwin says to Rogers, "I think I would sell my house for $1500." Rogers says, "I accept that offer." This does not create a contract because Baldwin's statement is not an offer.

3. Murphy says to Hawley, "I will pay you seventy-five dollars to paint my house." Hawley replies, "I will accept for ninety dollars." This does not

* Consideration is the thing of value which is transferred from one party to the other at the time of making the contract. It may be money, a thing, or a promise. Subject matter is that about which the agreement is made.

create a contract, because Hawley has not accepted Murphy's offer. He has changed the terms of the offer and has in reality himself made a new offer — an offer to paint the house for a larger sum.

### EXERCISE

**Illustration.** Ames meets Bates on the street and offers Bates his watch for $10.00. Bates takes the watch and pays Ames the $10.00.

In this case Ames and Bates are the parties; the agreement is for the exchange of property, and is mutual; the consideration is $10.00; and the subject matter is Ames' watch.

Analyze the following examples of common forms of the contract relation, and select in each example the four necessary elements—parties, mutual agreement, consideration, and legal subject-matter.

1. Mrs. Brown goes to the Acme Company and purchases a sewing machine for twenty dollars.
2. Black has contracted to build a house for Simpson for the sum of $3000.
3. Mellen purchases a ticket from the local agent of the C. B. & Q. Railroad Company from Chicago to Minneapolis, paying the sum of $10.22.

The detailed rules governing offer and acceptance are discussed in a later chapter. For the present we shall continue to view a contract as an offer by one party which has been accepted by the party to whom it was made. We shall now examine some of the features common to all contracts.

**21. Further Classification.** Even though we recognize an accepted offer, which creates a contract, we may still know little about a contract unless we determine its

1. Validity,
2. Solemnity, or manner of execution,
3. Mode of expression,
4. Time of performance,
5. Relation to each other of parties on the same side.

These will be discussed in order.

**22. Validity of the Contract.** Frequently persons try and intend to make a valid contract and fail in their attempt because they have neglected to comply with some rule which they should have observed. In that event their contract may be void, voidable, or unenforceable.

If *void*, it has no standing whatever in the eyes of the law, and is without effect of any kind from the beginning. The parties to it have wholly failed to create any new rights, but stand in precisely the same position as if they had never attempted to make a contract.

If *voidable*, it may be set aside at the pleasure of one of the parties who exercises a right which the other party does not have. A voidable contract may be carried out if the injured party desires to do so; but it is not a valid contract, in the proper sense of the term, because one of the parties may legally refuse to carry out the agreement. If he does refuse, the other party is without power to compel him to perform.

If *unenforceable*, it will not be enforced by the courts if either party objects. An accepted offer may possess all the elements of a valid contract, and yet there may be some statute applicable to this particular case which the makers have failed to observe, and because of this failure neither party can compel the other party to perform his part of the agreement.

EXAMPLES

**Void Contracts.** 1. Poole, a dealer in lard, formed a scheme to "corner the market" by securing control of the supply of lard and raising the price. He employed Leonard to carry out the details of the scheme. When Leonard sued Poole for his wages, the court refused to allow him to recover. Such contracts are designed to restrain trade, and are illegal and *void*. Leonard vs. Poole, 114 N. Y. 371.

**Voidable Contracts.** Smith, aged seventeen, offers to buy a horse from Morgan for $200. Morgan accepts the offer. If Smith thereafter refuses to take the horse and pay the money, Morgan can do nothing. This is because Smith was not twenty-one years old when he made the contract, and it is a rule of law that persons under that age, who are called minors, cannot be bound by contracts against their will. The contract in this case is not void, but *voidable*. If Smith desires to do so he can perform the contract.

**Unenforceable Contracts.** Johnson offers to sell his farm to Mahoney for $5000. Mahoney says, "I accept," but the parties do nothing further. Contracts to sell real estate are not enforceable by action unless some memorandum is made in writing signed by the parties. If either party refuses to perform his part of the contract, the other party cannot go into court and recover anything — the contract is unenforceable.

**23. Solemnity.** When persons desire to make a contract, they must first decide whether to make (1) a contract under seal, or, (2) a parol, or simple contract.

**A contract under seal** exists when the parties have written their agreement and placed opposite their signatures a seal. The presence of this seal gives to the contract a formality which it would not otherwise possess. This is because the courts decided at an early time that if the parties to a contract chose to perform this extra act, they showed a deliberation and an intent that the contract should be enforced if possible. It was therefore said that such contracts under seal would be enforced regardless of the presence or absence of any consideration. The contract under seal derived its validity from the presence of this seal alone and not from the presence of a consideration.

Shakespeare's Seal

Seals are of ancient origin; they are mentioned often in the Bible.* When few people were able to write even so much as their own names, a seal was used instead of a signature. The body of the contract was written for them by a public writer, and a drop of molten wax or a thin plate of wax, called a wafer, was placed at the end, and the imprint of the maker's seal was made upon it. In order to have the seal always with him, ready for instant use, the owner of it often had it engraved upon a ring. Seals are often indicated by a scroll inside of which the word "Seal" is written or typewritten.

The necessity for seals has long ceased to exist, yet when called upon to determine the rights of parties to a contract the courts of most states will recognize a difference if the contract be under seal. This difference will be more particularly noted under our later discussion of Consideration in Contracts.

For the present it is sufficient to say that a contract under seal is the only formal, or solemn kind of contract known to the law, and that its use at present is confined almost exclusively to contracts for the sale and transfer of land. In such cases the seals usually appear in one of the following forms:

*Name of party to be written here* ..... SEAL

or

*Name of party to be written here* ..... L S

* I Kings, Chap. 21. Daniel, Chap. 6. Esther, Chap. 8. Jeremiah, Chap. 32.

**Contracts by parol** (parol, a French word meaning "word, or promise") are all contracts not made under seal. They depend for their validity upon the presence of a legal consideration. They may be by word of mouth or in writing. It is preferable to make all contracts in writing, because thereafter there can be little opportunity for dispute as to the exact words used, but written parol contracts have no greater solemnity than oral ones. Throughout our treatment we shall designate parol contracts as *simple* contracts, because no particular formality is necessary in their execution.

EXAMPLES

1. Crookshank offered to employ Burrell to repair a wagon and promised to pay him $25. Burrell accepted the offer and did the work. The entire agreement was verbal. This was a valid parol, or simple, contract. It was also an oral contract. Crookshank vs. Burrell, 18 Johnson (N. Y.) 58.

2. Shores offered to sell some growing timber to Emerson, who accepted the offer, and the parties signed the following writing:

"This is to certify that I have sold the timber growth on my fifty-acre lot to Emerson for $85. Signed — C. D. Shores,
Accepted — Stephen Emerson."

This was a valid parol, or simple, contract. It was also a written contract. Emerson vs. Shores, 95 Maine 237.

**24. Mode of Expression.** Contracts may be either (1) express, or, (2) implied.

**An express contract** is one whose terms are stated and agreed to by the parties. It may be either written or spoken.

**An implied contract** is one whose terms are inferred from the *acts* of the parties.

EXAMPLES

**Express Contracts.** Burr offers to construct a woodshed for Abrams for $200. Abrams accepts the offer, and Burr proceeds with the building of the woodshed. Abrams thereupon becomes bound to pay Burr the agreed price.

This result will follow regardless of whether the contract was written or entirely oral. It is a simple express contract, and if Burr performs his part, *i.e.*, the construction of the woodshed according to agreement, then Abrams becomes liable to pay the $200, even though it should afterwards develop that the work was only worth $125.

It is to be noted in this connection that in express contracts the parties are bound by the terms in which they make their offer and acceptance.

**Implied Contracts.** 1. Jones, being ill, telephones Dr. Brown to come and attend him. Dr. Brown does so and on Jones' recovery sends him a bill for $500 for services. Although no actual express contract was made, Dr. Brown can collect this $500 provided his charge is a reasonable one.

This result follows because the law *implies* a promise on the part of Jones to pay the reasonable value of Dr. Brown's services, for it was at Jones' request that the services were rendered. Jones is not held, however, to pay whatever Dr. Brown may choose to charge, but only to pay a reasonable charge. That is the only contract which the law will *imply*.

2. Adams, who is going away for the summer, calls across to his neighbor, Moore, and says, "You might turn your hose on my flowers once in a while, Moore, if you feel like it." Moore does so, and on Adams' return presents a bill for $25. Here no contract will be *implied*, because the whole transaction will be viewed as a neighborly act for which no pay was intended, or expected. As there was no express contract, and as the law will not imply a contract from the acts of the parties, Adams need not pay the bill.

The ordinary contract of a business man is a simple, express contract. It is this kind of contract which we call to mind when we speak of the subject, "Contracts." Yet from the above examples it is to be observed that it is just and proper in many cases to have the law imply a contract, even though there may have been no verbal or written offer and acceptance. Implied contracts are not, however, the ordinary medium of business, and exist only when the acts of the parties show strongly that they must have intended to create a contract. The law will imply such contracts only in the interest of justice.

**25. Time of Performance.** Contracts may be either (1) executed, or, (2), executory. They are *executed*, when they are completely performed and nothing remains to be done. They are *executory* when any condition which either party has agreed to perform remains unperformed.

EXAMPLES

1. Ames and Bates agree to exchange horses. If they make the exchange immediately, the contract is *executed*, because everything is done which each party has, by the contract, agreed to do. Thereafter Bates has the horse which originally belonged to Ames. He owns it and keeps it in his stable. Ames has no rights over it. And similarly with the horse which Bates formerly owned, and which by the contract has become the property of Ames.

2. If, in the above example, the parties agree to exchange horses the Monday following, the contract will remain executory until the time of performance, *i.e.*, Monday. During the time when the contract remains executory, Ames keeps his own horse, and Bates keeps his. Each has acquired

merely the right to have the other's horse at a later date, called the time of performance.

On account of this difference in the effect of an executed and an executory contract, it is stated by one of the earliest of English law writers (2 Blackstone's Commentaries, 443) that an executed contract conveys a thing in possession (the horse, in the first example above); while an executory contract conveys a thing in action (the right of each to have the other's horse at the end of the week, in the second example above.)

The time of performance of a contract depends entirely upon the agreement of the parties. It is important because it determines the time when an executory contract should become executed.

**26. Relation to each other of parties on same side.** While a contract must from its nature have two parties, there may be more. As many persons as desire may, on the one side, contract with either a single person, or a number of persons on the other side. Ames, Bates, and Call may contract with Dale to build the latter's house. The first three are the parties of the one side, and Dale is the sole party of the other side.

If there are two or more parties on the same side of a contract, that is, who have contracted together on one side of a contract, a new relation is created. They not only have an obligation which they have agreed to perform as to the party, or parties, on the other side of the contract, but they have certain rights and duties as between themselves. Their obligations may be either *joint*, or *several*, or *joint and several*.

A *joint* obligation exists when all the parties on one side of a contract agree to act as a single person. Thus in cases in which the subject matter of the contract is entire, such as a sum of money which is to be paid to a number of specified persons, it is a joint contract as to those persons. The effect of a joint contract is that no single one of the persons contracting jointly can sue alone, or be sued alone, for his share. All joint contractors must join, or be joined together, when the contract is sought to be enforced in court.

If, however, the contract be to pay to each person a specific sum, or one in which each agrees to perform distinct and separate duties, the contract is said to create a *several* obligation. In such a contract any one of the parties may sue or be sued alone

for his share. Such a contract would exist in case A, B, and C agreed to pay $500 to D, A to pay $250 of the amount, B $150, and C $100.

When, in a written contract, the words, "I promise," or "We, or either of us, promise," or "We bind ourselves and each of us," are used, the obligation is *joint and several* and any failure to perform the agreement makes possible a suit against all those who promised jointly, or against one or more severally. A joint and several obligation is the most favorable to the person to whom it is made and the most unfavorable to those who make it, because any one of them may be compelled to carry out the whole agreement. The old common law idea was that all contracts were deemed to be joint, unless the parties specified that they should not be. This view has been changed by the statutes of some states, so that in them it is presumed that all contracts are joint and several, unless it be shown that the parties specified some other relation.

EXAMPLES

1. A group of shareholders in a corporation agreed with Marie to transfer their shares of stock to him and accept in return shares in a new corporation, or a sum of money. Marie failed to pay them for their shares as agreed, and when they sued him the court said that the obligation was *joint* and that they must all sue him together, because he had agreed to pay them all and not each one severally. The nature of the arrangement was such that the shares might be without value to him unless he received all of them. Marie vs. Garrison, 83 N. Y. 14.

2. Four persons bought a printing press for $1500, payable in four installments, each party agreeing to be responsible for one-fourth of the entire sum, or for one installment. One of them was sued alone for his particular installment, and the court said that this was proper because the obligation was *several* and not joint, and no one person could be held liable for more than one-fourth. Larkin vs. Butterfield, 29 Mich. 254.

3. In the last example above if the four persons who agreed to pay for the printing press had signed an agreement as follows: "We, the undersigned persons, or either of us, promise to buy, and pay $1500 for a printing press, in four installments," then any one of them would have been liable for not only a single installment, but for the entire purchase price, and the contract would have been *joint and several.*

**27. Effect of Death of Joint Contractor.** Upon the death of a person all debts for which he is individually liable "survive" against his estate, that is, they are payable out of the property

which he owned at his death. If the deceased was one of two or more parties on the same side of a contract, the liability survives against his estate if the obligation was a *several* one, or was *joint and several*. If the obligation was *joint*, the estate by common law is discharged from liability, but such cases are rare, since the tendency of courts is to regard all contracts where there are two or more parties on one side as *joint and several*. Some states, notably Massachusetts, New York, Ohio, Tennessee, and Wyoming, have declared by statute that even joint debts survive against the estates of deceased debtors.

ALLEN

## CHAPTER IV

### COMPETENT PARTIES

All parties are competent except:

- I. Mentally Incompetent
  - 1. Insane Persons
  - 2. Intoxicated Persons
  - 3. Spendthrifts
- II. Legally Incompetent
  - 1. Infants
  - 2. Married Women
  - 3. Aliens
  - 4. Agents (certain contracts only)
  - 5. Corporations (certain contracts only)

**28. Who Are Parties.** Persons who create, or attempt to create, new rights or obligations in themselves or others by means of a contract, are the parties to it. Ordinarily all persons capable of transacting business may make valid contracts. Exceptional classes of persons, however, are particularly designated by law as being incapable of making contracts, and their attempts to do so result merely in creating voidable, and sometimes void, contracts. Such parties are said to be incapable of making mutually enforceable contracts, because of *disabilities*.

**29. Disabilities.** A disability to create valid contracts may exist for either of two causes. These are (1) that the party is *mentally* incapable, or (2) that the party is *legally* incapable.

The affairs of such persons may be placed in the hands of a guardian (sometimes called a conservator) by order of court.

**30. Mental Incapability.** If persons who are mentally incapable of protecting their own interests, are parties to contracts, such contracts are not enforced against them, but are voidable at their option. Such persons are those who are (1) insane, (2) habitual drunkards, and (3) spendthrifts. The result of attempts by such persons to create contracts is explained by the examples under the next section.

**31. Insane persons.** *Insane* is a general term applicable to any person who is of unsound or deranged mind. It may indicate absolute loss of reason, or partial lunacy. The latter condition is frequently caused by grief, sickness or accident, and the mental capacity of the person may be restored by proper treatment or by the lapse of time. *Idiot* and *imbecile* are terms applied to persons whose mental development has been arrested. Insanity as a defense to a contract must be such that the party could not comprehend the force of his act.

The effect of an attempt by insane persons* to create a contract results only in creating an apparent obligation which is voidable. Such contracts may be either ratified or disaffirmed by the insane person on recovering his sanity, or by his guardian, but unless ratified cannot be enforced by the other party. Two exceptions to this general rule exist. The first exception is that insane persons may make valid contracts in their lucid intervals; the second, that they may create implied contracts to secure the necessaries of life.

If a party to a contract wishes to escape liability on the ground that he was insane when he made it, he will have to prove his insanity. If a person has actually been declared insane by the court, and thereafter attempts to make a contract, which the other party attempts to enforce against him, the party attempting to enforce the contract must prove to the court that the insane person had a lucid interval when the contract was made, or ratified.

It would be unfair to insane persons to destroy their right to secure the necessaries of life. In such instances, the court allows the party who has furnished the necessaries to recover the reasonable value. The party furnishing such articles to an insane person must show to the court (1) that they were necessary, and (2) their reasonable value. He cannot recover what the insane person agreed to pay, but merely what a reasonable

* In regard to contracts with an insane person, note the following rule, which is not applicable to contracts made with other persons under disability: If a party contracts with an insane person, without knowledge, or reasonable suspicion as to the other's insanity, the contract is valid and not voidable, *provided* the contract has been executed and the parties cannot be restored to their original position. Bollnow vs. Roach, 210 Ill. 364, 71 N. E. 454. If the contract is executory, or the consideration can be restored, it may be avoided by the insane person, or his guardian.

man, under all the circumstances of trade and commerce, would consider they were worth. Furthermore, if the insane person had a guardian, a party who attempts to recover the value of necessaries must also show that the guardian had failed in his duty to provide them.

EXAMPLES

1. Ames, a merchant, sells a piano, an automobile, and a barrel of flour, to Bates, who promises to pay for these articles $400, $2000, and $7, respectively. He fails to pay and when Ames sues him he proves to the court that he was insane when all these sales were made. The piano was worth $500, the automobile worth $2000, and the flour $6. Bates did not need either the piano or the automobile. Ames may recover only $6 for the flour.

2. A, a merchant, sold goods to B, which were suitable to his needs and his station in life, after B had been legally declared insane and C had been appointed his guardian. C was in Europe at the time, and had failed to make provision for B. On C's return he refused to pay for them, and A sued him. The court said that he must pay the fair value of the goods out of B's money, which he held. Fitzgerald vs. Ree, 9 S&M (Miss.) 94.

3. The question in all cases in which incapacity to contract because of defect of mind is set up in defense, is, not whether a person's mind is generally impaired nor whether he is afflicted by any form of insanity, but whether the powers of his mind have been so affected by his disease as to render him incapable of transacting business like that in question. Dennett vs. Dennett, 44 N. H. 531.

**32. Intoxicated persons.** Slight intoxication of one of the parties to a contract has no effect on the validity of the contract, but if a party is so completely intoxicated at the time of making a contract that he could not act intelligently, or was incapable of knowing what he was doing, the contract is voidable. It is extremely difficult for a person to escape his contract on this ground, unless he can prove that the other party took advantage of his condition.

EXAMPLE

Van Wyck sold his farm to Brasher for a fair price, having been attempting for a long time to sell it to others. Later he attempted to recover the farm, and offered to return the money, showing that he had been drinking heavily the day he sold it. Brasher showed that Van Wyck's real reason for wishing to recover the farm was that he had an opportunity to sell it to someone else at a higher price, land values having increased after the sale. The court refused to return the farm to Van Wyck, and said there was no proof that Brasher had taken advantage of him. Van Wyck vs. Brasher, 81 N. Y. 260.

Habitual drunkards may be placed in the care of guardians appointed by the court, and in that event the duties of the guardian, and the rights of third persons furnishing necessaries, are the same as in the case of insane persons.

**33. Spendthrifts.** A guardian may also be appointed to care for the business affairs of a person who is so dissolute in his habits, or so lacking in judgment* as to be incapable of properly caring for his own property. Such a person is called a spendthrift. If a guardian is appointed, his duty, and that of third persons furnishing necessaries, is the same as that of a guardian of an insane person. The right to appoint a guardian for a spendthrift depends upon the statutes of the different states.

**34. Legal Incapacity.** Certain types of persons are specifically designated by the law as incapable of making valid contracts. In some instances, they are totally prohibited from contracting, and in other instances they are allowed to contract, under certain conditions, and subject to certain limitations. Persons whom the law declares to be either totally or partially incapable of making contracts are (1) infants, (2) married women, (3) aliens, (4) agents, and (5) corporations. Particular rules, which are discussed in the following paragraphs, exist for each class.

**35. Infants.** An infant is a person who has not reached a legal age, which is the age fixed by law as that at which he should have arrived at years of discretion, and be capable of safeguarding his own affairs. At common law this age is twenty-one years for both sexes, but by statutes in many states the legal age for women is reduced to eighteen years.†

**36. Voidable Contracts of Infants.** The general rule is that an infant is not competent to bind himself by contract, except for necessaries, and that he may avoid any contract made

* Aged persons frequently lose their mental faculties and became incapable of caring for their own property. In such cases, a guardian may be appointed for them, with the same effect as in the case of spendthrifts.

† Alabama, Arkansas, Colorado, Connecticut, Delaware, Georgia, Illinois, Indiana, Iowa, Michigan, Minnesota, Montana, Mississippi, Maine, Maryland, New Jersey, New York, New Hampshire, Nebraska, Ohio, Nevada, Oklahoma, Oregon, Rhode Island, South Carolina, North Carolina, Texas, Utah, Wyoming, Wisconsin, Washington.

by him during infancy. This is true even though he may have been self-supporting and living apart from his parents. It is to be observed that the infant is the party whom this rule of law seeks to protect and therefore the defense of infancy is open to him alone and not to the other party with whom he contracted. It is therefore said that the contracts of an infant are voidable "at his election," and may be ratified or disaffirmed by him.

**When Necessary to Ratify.** If a contract made by an infant is executory, or unperformed, when the infant attains his majority, it is void unless ratified by him at that time or within a reasonable time thereafter. Failure to disaffirm will not be sufficient; there must be a positive ratification.

**When Necessary to Disaffirm.** If a contract made by an infant is executed, it is necessary for the infant to disaffirm it, at the time of reaching his majority or within a reasonable time thereafter, if he wishes to avoid it. Failure to ratify will not be sufficient; there must be an express disaffirmance. Until such disaffirmance the contract has a *prima facie* validity.

EXAMPLES

1. Clemmer, 19 years of age, executed a contract which he had previously made, by paying Price $2,000 for his farm. Clemmer took possession of the farm, but five years later offered to return it and demanded that Price repay the $2,000. The facts were presented to a court which ruled that as the contract was executed and had not been expressly disaffirmed within a reasonable time after Clemmer became 21 years of age, it could not be set aside, but was binding between the parties. Clemmer vs. Price, 125 S. W. (Tex.) 604.

2. Morton, an infant aged 20 years, promised in writing to pay Steward $90 for a horse two years later. Nothing further was done until the two years had elapsed, when Steward offered to deliver the horse and demanded the $90, which Morton refused to pay on the ground of his infancy at the time the contract was made. The court ruled that this was a good defense as there had been no ratification and express disaffirmance was not necessary to avoid executory contracts of infants. Morton vs. Steward, 5 Ill. App. 533.

If an infant disaffirms an executed contract within a reasonable time after attaining his majority, he cannot ordinarily recover his property or goods without first restoring the property or goods which he may have received from the other party. If he no longer has these goods he must in some instances pay the other party their value, though the courts are by no means uniform in the several states in applying these rules.

If an infant desires to ratify an executory contract on attaining his majority, he must ratify the *whole* contract, and not merely a part. Thereafter his liability is treated as complete and binding from the beginning.

EXAMPLES

1. Bardwell, an infant, contracted with Wallis who agreed to build an addition to the infant's house, for which the infant promised to pay a stated sum. Later the infant refused to pay for the work, and the court said that this work (which was the building of a new porch) was not necessary, and allowed no recovery. Wallis vs. Bardwell, 126 Mass. 366; Bloomer vs. Nolan, 36 Neb. 51.

2. A, an infant, needed money to complete his education, and sold his house to B, who paid a fair price. After A reached legal age he found he could then sell the house for a larger price and notified B to give it back to him, offering to return the price B had paid. This B refused to do, but A nevertheless proceeded to sell the house to C, who sued B. The court gave C the house, saying that A had exercised his right of election promptly. Shipley vs. Bunn, 125 Mo. 445; Dixon vs. Merritt, 21 Minn. 196.

3. Young, an infant, purchased land from Potter and paid the agreed price. He then contracted to sell the same land to Carrell, who promised to pay him $250. After arriving at legal age, the infant continued to keep the land and refused to convey it to Carrell or to accept the purchase money. Carrell sued him, but the court allowed the infant to keep the house, since he had made no act of affirmance after reaching twenty-one. Carrell vs. Potter and Young, 23 Mich. 377.

**37. Infants' liability for necessaries.** An infant, however, owes the same duty to pay the reasonable value for the necessaries of life which he has received, as exists in the case of insane persons. It is necessary for a person who sues an infant for the value of necessaries to show to the court that the articles were actually necessary in the light of all the circumstances of the case. What may be a necessary to one person may be a luxury to another. If it can be shown that the articles furnished an infant were actually necessary, the person furnishing them may collect the reasonable value, but not the price which the infant promised to pay, if this was more than the reasonable value.*

* The student should here note, however, that a person suing an infant, even though he may be able to recover a *judgment* for the value of the necessaries, may be unable to collect any money, because the infant may own no property. In such cases the judgment is without money value until the infant acquires property of his own.

EXAMPLE

Archer, an infant, receives from Jones, a grocer, some potatoes for which he promises to pay $2.00. Archer is living alone at the time and uses the potatoes for his meals. The potatoes are actually worth only $1.50. In a suit against Archer, Jones can recover only $1.50.

Jewelry, walking-canes, liquor, tobacco, bicycles, a saddle and bridle, in certain cases have been declared by courts to be unnecessaries, in the light of the particular facts. Under other facts, including the infant's station in life, a watch, wedding clothes, school books, a microscope, dental service, and room-rent, and in some cases even some of the articles enumerated in the preceding sentence have been declared to be things for which the infant should be compelled to pay the reasonable value, being necessaries.

**38. Married women.** Married women now generally have the same rights to make contracts in their own name, to hold real and personal property, and the use their earnings, as they had before marriage.* A married woman may also make contracts by which she may bind her husband to pay for necessaries, but not other articles, unless she is acting as his agent, in which case she is subject to the same limitations as other agents. (See section on agency.)

At common law a married woman was not capable of making a valid contract, and was therefore not liable on any contract which she might make; neither could she enforce it. The common law idea was that when a woman married, all her property, rights, and even her separate existence became bound up, and merged, with that of her husband, who alone was deemed capable of engaging in business. The contracts of married women were absolutely void, and not merely voidable as in the case of infants. This harsh view has been changed by statutes in the various states, so that little is left of the old rules.

**39. Aliens and Alien Enemies.** A contract made with an enemy in time of war is illegal and void, both at common law and under many state statutes. This principle was applied to many contracts made during the Civil War.

There are laws in many of the states restricting aliens' property rights.† These serve as a restriction on their power to acquire many property rights by contract, or otherwise.

* Women under legal age, though married, may avail themselves of the defense of infancy, unless living in a state whose statute specifically declares them of age at marriage. Such states are: Iowa, Oregon, Washington.

† Aliens have the same property rights as do citizens in Alabama, Colorado, Indiana, Iowa, Maryland, Massachusetts, New Jersey, Alaska, Florida, Georgia, Maine, Michigan, New Mexico, North Carolina, North Dakota, Ohio, Oregon, Rhode Island, South Dakota, Tennessee, Utah, Wyoming.

**40. Agents.** An agent is one who acts for another, in making such contracts as he has been authorized to make. He is not personally liable for his acts if he makes only such contracts as he was authorized to make, and he binds only the person who so authorized him (called the *principal*). (See chapter on agency.)

**41. Corporations.** A corporation is a form of business organization which may act in many ways like a natural person. It may only perform such acts, however, as it is specifically empowered to do by statute, and then only in the particular manner which the statute permits. A complete treatment of this subject is presented in the chapter on Corporations.

## PRACTICAL SUGGESTIONS

Don't contract with persons whom you fear to be mentally or legally incompetent, *because* you do so at your peril.

Don't sell goods to married women and charge the items to their husbands unless you are certain the goods are necessaries, or know the husband will pay regardless of his legal rights, *because* you cannot make him. The husband's consent is sometimes easier to get before the sale, than after.

Avoid selling any goods on credit to infants except necessaries, unless you are willing to rely upon the good nature of the parents to pay their children's bills, *because* you create a contract which is binding on you alone.

It is improvident to buy real estate from an incompetent person, without a court order, *because* if the value goes up he may want it back, and can get it.

Don't, if in spite of this advice, you feel that you must do business with an incompetent person, take any advantage of his condition, *because* the court will protect him and censure you.

Don't sue incompetent persons without consulting your lawyer, *because*, even though they may be legally liable, you can sue them only by following a complicated legal procedure.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1., Sands, a dealer in butter and cheese, entered into a written contract whereby he agreed to employ Potter for three years and in addition to paying him wages, agreed to give him a share in the profits. At the end of three years he paid the wages, but refused to pay the one-half of the profits. Potter sued Sands, who defended on the ground that he was insane when he made the contract. The court declared that Sands at the time he made the contract, was insane, but that "he was then possessed of mind, memory, and senses sufficient to know and comprehend the scope, force, and effect of the particular contract." Can Sands escape from paying Potter a share of the profits? Why?

2. Wanamaker sued Weaver for the purchase price of a dress which he had sold to Mrs. Weaver. This was the first time the Weavers had ever purchased anything of Wanamaker. It was admitted that dresses were ordinarily necessary articles, but Weaver showed to the court that his wife had more dresses than she needed before she made this purchase. Can Wanamaker recover the price of the dress from Weaver? from Mrs. Weaver? Why?

3. Jonas, a real estate dealer, was particularly acute in business when intoxicated. One day when he was so intoxicated that no one believed he knew what he was doing, Baldwin, believing he could take advantage of Jonas in this condition agreed to buy Jonas' farm for $9000. This was really $3000 more than it was worth, though Baldwin did not know it. Later he discovered this fact and refused to take the farm on the ground that Jonas was so intoxicated at the time he made the contract that he did not know what he was doing. Was there a contract? Why? Can Jonas make Baldwin take the farm? Why?

4. Mahoney, who claimed to be Christopher Columbus whenever he saw a ship, and Simpson, who believed himself to be married although he was not, were both conducting real estate business. Aside from these peculiarities, each was looked upon as a sound business man. Mahoney agreed in writing to sell Simpson a house for $5000, which Simpson agreed to buy. Later Mahoney discovered that the value had advanced and refused to carry out the contract. Was there a contract? Why? Has Mahoney a good defense? Why?

5. Jacob Schneider, an infant, bought some shoes of Bule, a dealer, for which he promised to pay two dollars. A year later he became of age, and on being asked to pay by Bule, stated that he considered his obligation binding on him and would pay shortly. Later he refused to pay altogether and was sued by Bule. The reasonable value of the shoes was one dollar and twenty-five cents. What amount, if any, can Bule recover? Why?

## CHAPTER V

## THE AGREEMENT

- I. Common Intention to Create Contract
  - 1. Real
  - 2. Unreal
    - a. Mistake
    - b. Fraud
    - c. Duress
    - d. Undue Influence
- II. Offer
- III. Acceptance

**42. Mutuality.** There can be no contract in the true sense, as distinguished from an implied contract, unless there is an accepted offer. At the moment the offer of one party is accepted by the party to whom it is made, there is a meeting of the minds of the parties. This meeting of the minds is called *mutual assent*, and the presence or absence of this mutual assent determines whether or not an agreement exists.

**43. Agreement. Its Essentials.** An agreement, therefore, exists when two or more parties assent to be bound by a contract. Its essentials are:

1. A common intention to create a contract;
2. A communicated offer;
3. An unqualified acceptance.

The conception of a contract as an accepted offer makes it necessary that there be at least two parties. A person cannot enter into an agreement with himself so as to create this legal relation, called contract. He may make as many New Year resolutions as he likes, but these are not contracts, because the law will not enforce them.

**44. A common intention to create a contract.** Not only must there be at least two parties, but these parties must have a common intention to enter into the contract relation. Even though the offer be formal and complete, it cannot be the foundation of an agreement if it was made and accepted with no intention to create a contract but as a mere jest or joke.

EXAMPLE

Holderman wrote out a bank check for $300.00 and gave it to Kellar in payment for Kellar's watch, worth $15.00. It was proved that the whole transaction was carried on in sport. This did not create an agreement, and Holderman could not keep Kellar's watch, nor could Kellar collect the $300.00. Kellar vs. Holderman, 11 Mich. 248.

## OFFER

- 1. Unconditional
- 2. Conditional
  - a. As to Time of Acceptance
  - b. As to Place of Acceptance
  - c. As to Manner of Acceptance

**45. A communicated offer.** Not only must there be two or more parties with a common intention to create the contract relation, but one of the parties must communicate to the other a definite offer. The party making the offer is called the *offeror*; the party to whom it is made is called the *offeree*. The offer made by the offeror consists of some statement, or some act, by which he indicates to the other party, the offeree, three things. These are: (1) the offeror's desire to create a contract, (2) the terms of the contract which he is willing to make, and (3) the manner in which he desires his offer to be accepted. In other words, an offer is the expression by one party, who desires to create a contract, of the terms by which he is willing to be bound.

EXAMPLES

1. Compton said to Stagg, "I mean to sell this property if I can get $100.00 for it." Stagg replied, "I will give you $100.00 now." This did not create a contract, because Compton's statement showed no present desire to create the contract relation. Compton vs. Stagg, 81 Ind. 171.

2. Paige's wife was in a burning building, and Paige called out to a crowd of men standing nearby, "I will give $1000.00 to anyone who will bring out my wife's body." Reif, a fireman, at the risk of his life brought out the body, thereby complying with the terms of the offer. This created a contract, and Paige was bound to pay the $1000.00. Reif vs. Paige, 55 Wis. 496.

3. A steel mill offered to sell a railroad 5000 tons of iron rails at a certain price, providing in the offer, "if accepted, we shall expect to be notified by December 20." This constituted a condition which the offeror imposed on the offeree, *i.e.*, acceptance within a specified time. Minneapolis & St. Louis Railway Company vs. Columbus Rolling Mill, 119 U. S. 149.

**46. Offer May Be Conditional.** Not only may the offeror make his offer in a variety of forms, but he may attach as many conditions as he pleases. He may limit the means, the manner, and the place of acceptance, provided the offer does not thereby become so uncertain as to be meaningless. When a conditional offer is made, the person to whom it is communicated can accept it so as to create a contract, only by complying with all the conditions contained in the offer. The most usual conditions attached to offers are that they be accepted, if at all, within a given time; or in a given manner, as by mail, telegraph, or telephone; or at a given place, as Chicago, New York, St. Louis.

ACCEPTANCE

- I. Form
  - 1. An Act
  - 2. A Promise
- II. Quality—Unconditional
- III. Communication
  - 1. Before Revocation of offer
  - 2. After Revocation of offer
    - a. By Notice
    - b. By Lapse of Time
    - c. By Operation of Law

**47. Acceptance of Offer.** An offer is without legal effect, and may be withdrawn at any time before the person to whom it is made, the offeree, has accepted it. Acceptance is therefore the assent of the offeree to the offer of the offeror. Acceptance may be made either (1) by a promise, or (2) by an act.

EXAMPLES

**Acceptance by a promise.** A water company offered to extend certain water mains if a lumber company would agree to pay $250.00 a year for ten years. The lumber company promised to make the payments. Muscatine Water Company vs. Muscatine Lumber Company, 85 Iowa 112.

**Acceptance by act.** 1. Graff and a number of other persons together signed a subscription paper in which they offered to pay a total sum of $10,000.00 to a designated railroad, provided trains were running by October 1, 1864. The railroad had trains running on that date. Des Moines Valley R. R. Company vs. Graff, 27 Iowa 99.

2. Cooper sent a quantity of leather to Orme, without request, and then wrote Orme offering to allow him to keep it at 20 cents a pound, or to take it

back and pay the freight. Orme did not answer the letter, but used the leather. The court decided that this act by Orme constituted an acceptance of Cooper's offer. The act in this case in reality consisted in Orme's taking the benefit after he knew that Cooper expected to be paid. Orme vs. Cooper, 1 Ind. App. 449.

**48. Sufficiency of Acceptance.** To create a contract, the acceptance must further

1. Comply with the conditions of the offer,
2. Be itself unconditional, and,
3. Be communicated to the offeror.

These elements of the sufficiency of an acceptance are illustrated in the following examples:

**Compliance with conditions of offer.** 1. A railway company wrote Lawrence offering to carry a certain quantity of logs for him at a certain rate, on condition that he would provide chains for the logs if necessary. Lawrence wrote back, "I accept your offer," saying nothing about chaining the logs. The court decided that by this general acceptance Lawrence agreed to comply with all the conditions of the offer; that a contract existed by which the railroad was compelled to carry his logs for the price; and that Lawrence was compelled to provide chains. Lawrence vs. Milwaukee, Lake Shore & Western Railway Company, 84 Wis. 427.

2. Snedaker posted a notice offering to pay $500.00 "to any person who will give such information as shall lead to the apprehension and conviction" of a certain murderer. Fitch performed the act of giving the information necessary to convict the murderer, but at the time knew nothing of the offer. The court decided that no contract was created. Even though one complies with the terms of an offer, one cannot thereby accept an offer of which one is ignorant. Snedaker vs. Fitch, 38 N. Y. 248.

**Acceptance must be unconditional.** 1. Brown wrote to Hough offering to transport Hough's freight from Chicago to New York by way of Boston for ten dollars a ton. Hough replied, "I accept your offer, with the understanding that if we ship direct to New York and not by way of Boston, you will charge us only nine dollars." This acceptance failed to create a contract. Hough vs. Brown, 19 N. Y. 111.

2. McCotter offered to sell to the city of New York all the land which he controlled on Ward's Island for a certain price per acre. The city council of New York passed a resolution by which it agreed to buy *all* of Ward's Island for the price per acre contained in McCotter's offer, and sent McCotter a copy of the resolution. The court decided that this varied the terms of the offer by imposing new conditions and failed to create a contract. McCotter vs. Mayor, etc., of New York, 37 N. Y. 325.

**Acceptance must be communicated to offeror.** Harvey made Maclay an offer, and Maclay wrote out an acceptance which he gave to a messenger

boy to take to the post-office. The messenger lost the letter of acceptance. No contract resulted from this act. Maclay vs. Harvey, 90 Ill. 525.

**49. Communication of Acceptance.** The offeror may designate the particular means by which he wishes acceptance to reach him, and if he does this an acceptance communicated in the manner specified is always sufficient. If no means of communication of acceptance be designated by the offeror, an acceptance by the same medium as that used by the offeror is always sufficient. In such cases the risk of the acceptance actually being received is upon the offeror, and the contract is made upon the delivery of the acceptance to the agency of communication selected, such as the government mail, the telegraph company, or the messenger who delivered the offer.

If the offeree communicates his acceptance through a medium other than that designated, or if in the absence of a designated medium, the offeree accepts through a medium not used by the offeror, the acceptance has no effect until it actually reaches the offeror, and even then can be refused if it does not reach him within a reasonable time.

EXAMPLES

1. Kempner at Hot Springs mailed to Cohn at Little Rock an offer to sell his house for $10,000.00. Cohn immediately, and on February 7, mailed a letter of acceptance, which because of the fault of the post-office department did not reach Kempner until February 10. In the meantime and on February 9, Kempner wrote Cohn withdrawing the offer. The Court decided that there was a valid contract between the parties, created on February 7. Kempner vs. Cohn, 47 Ark. 519.

2. Wood made Callaghan an offer by letter. He failed to receive Callaghan's acceptance of his offer, and claimed that no contract ever existed between them. Callaghan proved that he had deposited a letter of acceptance, proper in form, in a street letter-box. That was held by the court to be sufficient, the previous correspondence between the parties having been by mail. Wood vs. Callaghan, 61 Mich. 402.

If, however, the letter is not properly addressed (Potts vs. Whitehead, 20 N. J. Eq. 55), or is not stamped (Blake vs. Hamburg-Bremen Fire Insurance Company, 67 Tex. 160), no contract results unless the acceptance actually reaches the offeror within the proper time.

3. A mailed a letter accepting an offer which B had made to him by letter. Thereafter, A found that the contract would not be advantageous to him and telegraphed to B, declining the offer. The telegram was received by B before the letter reached him, but the court nevertheless said that a contract

existed between A and B from the time when A had deposited his letter of acceptance in the post-office. Halleck vs. Insurance Company, 26 N. J. Law 268.

Cancellations, even after acceptance has merged an offer into a contract, are frequently tolerated by business men, but the student must remember that such toleration is a matter of business policy, and not of law.

**50. Withdrawing the Offer.** Until an offer is withdrawn it may be accepted, and when accepted it ripens into a contract. Before acceptance takes place in one of the forms previously noted, the offer may be withdrawn by the party who made it. This is called *revoking* the offer. As no contract exists until the offer is accepted, it is logical and just that the party who makes it be permitted to change his mind, provided he notifies the offeree of the revocation before the offeree accepts it.

The revocation of an offer may be accomplished in one of three ways. (1) The offeror may expressly revoke his offer, in which case actual communication of the revocation* must be effected, except that if the offer was by public notice a revocation by the same means is effective. (2) The offer may be revoked by lapse of time. If the offer was made with a time limit, the offer is automatically revoked when the time expires. If no time was stated in the offer, the lapse of a reasonable length of time will effect revocation. (3) The offer is revoked by operation of law if the offeror dies or becomes insane before the offer is accepted, because there can then be no legal "meeting of the minds" of offeror and offeree.

**51. Unreal Mutual Assent.** Although the parties may have apparently created an agreement by mutual assent, through the medium of an accepted offer, there are two conditions under which the contract may be unenforceable for the reason that their apparent mutual assent was unreal. These are (1) when there has been a mistake of fact, and (2) when one of the parties would not have entered into the agreement except for the fraud, duress, or undue influence practiced upon him by the other.

**52. Mistake of Fact.** An agreement to be valid requires, as we have already seen, that the minds of the parties shall have met on the same subject matter, at the same time, and with the

* Dropping a letter in the post box will not be sufficient in this case. The letter must be actually received.

same intention. If any one of these conditions is lacking, there is a mistake of fact,* which will enable one, or both, to avoid the resulting contract. Such a mistake must be as to some material matter, and not merely as to a trifling detail, and may arise in one of three ways: (1) From the nature of the transaction; (2) concerning the person with whom the contract is made; or (3) concerning the subject matter of the transaction.

EXAMPLES

1. McGinn and Tobey intended to enter into a contract, the terms of which they had discussed. McGinn then wrote out the terms to which they had agreed, and also wrote out and sent to Tobey at the same time a second paper containing different terms, as an alternative proposition. Tobey signed both these papers, believing that they were duplicate copies of the agreement. No contract was created by the second paper, because there was a *mistake as to the nature of the transaction.* McGinn vs. Tobey, 62 Mich. 252.

2. Gordon, who had a bad reputation, advertised under the name of "Addison" that he had money to lend. Street read the advertisement and agreed by letter with "Addison" to borrow a sum of money and to pay "Addison" a commission for lending it to him. He would not have made any agreement with Gordon, on account of his bad reputation. On discovering his mistake, the court allowed Street to avoid the agreement, and he did not have to borrow the money or pay Gordon the commission for lending it to him. This was because there was *a mistake as to the identity of the parties.* Gordon vs. Street, 2 Q. B. (Eng. 1899) 641.

3. A agreed to buy, and B agreed to sell, at a specified price, certain cotton which the parties described as "cotton to be delivered ex Peerless from Bombay," referring to the steamship on which it was to be transported. There were, however, two ships named "Peerless," the buyer referring to one and the seller to the other. No contract resulted from this agreement, because there was a *mistake as to the subject matter of the transaction.* Raffles vs. Wichelhaus, 2 H. & C. (Eng.) 906.

4. Ames agrees to buy a house from Bates, which Bates agrees to sell. The house, however, has burned down before the making of the contract, without the knowledge of either party. This avoids the contract, because the

*A *mistake of fact* is to be distinguished from a *mistake of law.* A mistake of law occurs when a party misunderstands the legal effect of his word or acts. He cannot escape from a contract on this ground. Such a mistake occurred when A and B agreed to buy and sell, respectively, a house which the parties described as "being in first class condition." A, the buyer, thereafter refused to complete the bargain, claiming that he had always understood that the law would require B to repaint the house, and that he was mistaken. This did not excuse him, as a party to a contract is judged by his acts, and not what he believes to be the legal consequences of his acts. "Ignorance of the law excuses no one."

subject matter has ceased to exist. At the time of making the agreement both Ames and Bates believe the house to be in existence, and if it has been destroyed there is a mutual mistake as to the subject matter.

**53. The second kind of unreal mutual assent** arises by the wrongful act of one of the parties, which permits the other party to avoid the agreement. This wrongful act may be (1) fraud, (2) duress, or (3) undue influence. The presence of any of these elements makes the contract *voidable* (see Sect. 22), and the innocent party may refuse to carry out the contract.

**Fraud** is the wilful misrepresentation of a material fact. Mere exaggeration of the good qualities of the thing sold, or of the advantages of the proposed contract, does not constitute fraud. The other party must be on his guard against such exaggeration and must form his own conclusions of the merits of the proposition. If fraud be proved, it must be shown that there was a misstatement as to some actual fact, not merely an expression of biased opinion.

EXAMPLES

1. A and B were doing business together, and in order to get C to buy an interest in the business, they made false statements as to the profits which they had made during the preceding year. C relied on these statements and agreed to buy an interest in the business. Thereafter he discovered that the statements were false, and the court allowed him to refuse to buy or pay for the interest which he had agreed to take. Bower vs. Fenn, 90 Pa. St. 359.

*Note.*— If, in the preceding example, A and B had merely told C of the profits they expected to make in the future, and C had promised to buy into the business, the contract would not be *voidable*, because a statement concerning what may happen in the future is not a fact but an opinion, and there would have been *no wilful misrepresentation of a material fact.*

**Duress** is that which induces a person to perform an act, not of his own will, but because of the threats, or acts of violence, of some other person. Duress may be brought about by imprisoning, or threatening to imprison, a person wrongfully, or from an improper motive, or by threatening him with bodily injury, in order to compel him to enter into a contract. The threat or force must be sufficient to deprive a person of his free will, and sufficient to impress a person of average firmness of mind.

A owed B for some groceries. B wrote out a notice which stated that unless A gave him his horse and a sum of money, A would be put in prison for a long time. A became frightened and delivered his horse to B. He was

allowed to recover the horse, because he delivered it only because of the threat of B. Seiber vs. Price, 26 Mich. 518.

Other examples of duress are: Holding a gun at a man's head and compelling him to sign a contract; threatening to "beat you within an inch of your life unless you agree to this;" locking a person in a room until he accepts an offer made to him. Contracts resulting from such acts are voidable.

**Undue influence** exists when a person who occupies a position of confidence, or trust, toward another, takes an unfair advantage of his position, and thereby induces a contract. An attorney occupies such a relation toward persons who consult him; as also does a physician toward his patient. If such a person induces another to do some act, by means of statements of such a character that it is clear that the act is not voluntary, but is really the act of the person making the statements and not of the person performing the act, the contract resulting is said to have been induced by undue influence, and is voidable.

EXAMPLES

A young lady who had just become twenty-one years old consulted her uncle about all her business affairs. He induced her to sign an agreement that if a bank would lend him money, she would pay it if he did not. The uncle ran away with a large amount of money which he secured from the bank. The court said that the bank could not recover this money from the young lady, because her uncle had secured this agreement by means of undue influence and the bank, knowing the relation of trust existing, should have been on its guard. Rider vs. Kelso, 53 Iowa 367.

*Note.*— All contracts made between such persons are not voidable, however. If they are fair and just, they will be enforced, because in that event no one can say that they were induced by undue influence.

## REVIEW QUESTIONS

1. Perry in Rhode Island wrote a letter to an iron company in Boston, offering to sell five tons of boiler plate at a certain price. The iron company telegraphed to Perry, "We accept your offer; ship the boiler plate." This telegram was received by Perry. Did these acts create a contract? Why? Who was the offeror? the offeree?

2. A promised to teach B dressmaking if B would promise to work for her for six months. How may this offer become a contract?

3. The governor of Mississippi received the following telegram: "There are many cases of yellow fever at Cooper's Well; send out a physician this afternoon. Signed, I. Williams." The governor posted the telegram on a bulletin board, and Dr. Brickell, who saw it, went to Cooper's Wells, where he spent four days aiding the sick. He then sent a bill to Williams for $250 for his services. Was this proper? Was a contract created? Who was the offeror? the offeree?

4. A Chicago street car company posted the following notice:

"$5000.00

June 24, 1895.

"The above reward will be paid for the arrest and conviction of the murderer of C. B. Birch, who was fatally shot while in the discharge of his duties, on the morning of June 23d, at the car-barn. Signed, Charles T. Yerkes, Pres. W. Chicago Street R. R. Co."

Before the notice was posted an employee of the Company had given the police information which subsequently led to the arrest and conviction of the murderer. Did the employee have a right to secure the reward? Why? Was there an offeror in the above example? an offeree?

5. Henthorn called on Fraser in Liverpool and asked for an offer on some houses. Fraser handed him a written offer and Henthorn returned to his home in Birkenhead. The next day at one o'clock Fraser mailed a letter at Liverpool to Henthorn, withdrawing the offer. This letter did not reach Henthorn until five o'clock, and he at three o'clock had deposited a letter in the post-office at Birkenhead accepting Fraser's offer of the day before. Was a contract created? Why? Who was the offeror? the offeree?

## PRACTICAL SUGGESTIONS

### To Offerors

If you wish to limit the time in which an offer may be accepted, be sure to specify this limitation in your offer, because if you fail to do this the offer can be accepted within any reasonable time.

In making an offer, say exactly what you mean, *because* the offer may be accepted before you have an opportunity to explain. Then it will be too late.

Don't make an offer and then forget about it, *because* it may be unexpectedly accepted.

Don't wait until tomorrow to withdraw an offer if you have changed your mind, *because* the other party may make it a contract in the meantime.

### To Offerees

Don't change the terms of the offer by your acceptance, *because* no contract will result.

Accept an offer at once if the bargain is a good one, *because* the offer may be withdrawn.

Remember to stamp and properly address your letter of acceptance, if you mail it, *because* it may never be delivered and the fault will be yours.

In accepting an offer, use the designated medium of communication, if any; if not, use the same means of communication that the offeror used.

### In General

Don't fail to be clear in your language, preventing all chance of mistake, *because* your contract may be declared invalid on account of mistake.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## CHAPTER VI

## CONSIDERATION

- I. Simple Contracts
  - 1. Sufficient
    - a. Benefit to Promisor
    - b. Detriment to Promisee
    - c. Mutual Promises
  - 2. Not usually sufficient
    - a. Impossible
    - b. Moral Obligation Only
    - c. Past Consideration
    - d. Previous Obligation
    - e. Illegal
- II. Formal Contracts

**54. Consideration** is a benefit given to the party promising to do an act (who is called the *promisor*), or a loss or detriment suffered by the party to whom the promise is made (called the *promisee*). It is something given or done by one party to a contract, on account of which the other party agrees to perform his share of the obligation. The consideration for a contract, which must be present if the contract is valid, may exist in three different forms. These are,

1. A benefit received by the person making the promise, or someone in his behalf.

2. A loss or detriment suffered by the person to whom the promise is made, or someone in his behalf, or

3. The exchange of mutual promises between the parties.

*Note.*— The word *consideration* may mean the whole consideration, or a part of the consideration, however small. If anything be paid or done, it binds the bargain, whether more remains to be paid or done, or not.

**55. Benefit received.** If at the time of the making of the contract, the party who has made a promise to another receives

something for making the promise, this is said to be a *benefit to the promisor*. It does not matter how much or how little he receives, provided it is something of value.

EXAMPLES

1. Ames says to Bates, "I will promise to pay your expenses at the university next year, if you will pay me $500 now." If Bates pays the $500, Ames receives the benefit of having this amount at present, and a contract exists between the parties. The $500 is the consideration.

2. Call owes Dale $1000, which he will have to pay a year later. Egan says to Call, "If you will pay me $200 now, I will pay your debt to Dale when it falls due." When Call pays Egan the $200, this constitutes a legal benefit to Egan, even though he will have to pay five times this amount to Dale a year later because of his promise.

An exchange of one sum of money for another, both payments being made at the same time, does not come under this rule. In Schnell vs. Nell, 17 Ind. 29, the court held that an exchange of $600 for 1¢ left a balance due of $599.99, for which balance no consideration had been paid.

**56. Loss or detriment suffered.** The most usual form of consideration is some loss or detriment suffered by the person to whom the promise is made, or by some other person for him, in reliance on the promise. In the example under the preceding paragraph there is present, not only a benefit to the person making the promise, but also a loss or detriment to the person to whom the promise is made. This loss or detriment may take any one of a variety of forms.

EXAMPLES

1. John Bridgers owed a bank a large amount of money. The bank promised his wife that it would not sue him, if she would pay the debt out of her own money. This she agreed to do. By so agreeing she suffered a detriment, since she became bound to do something that she would not otherwise have been obliged to do. This consideration was sufficient to bind the bank to observe the terms of its promises. Bank of New Hanover vs. Bridgers, 98 N. C. 67.

2. An uncle promised his nephew that he would give him $5000 if he would refrain from drinking liquor, swearing, and playing cards or billiards for money until he was twenty-one years old. The nephew agreed so to refrain. This agreement constituted a detriment, because while it would have been better for the nephew not to have done these things any way, he could legally have done them before he agreed not to. A valid contract was created. Hamer vs. Sidway, 124 N. Y. 538; Talbott vs. Stemmens, 89 Ky. 222.

3. A agreed to pay B $100 if B would change his residence. B changed his residence, and thereafter A tried to avoid paying him the $100, claiming

that he had received no benefit from B's change of residence. The court said that a benefit to the promisor was not necessary, inasmuch as B, the promisee, had suffered a detriment by moving when he was not otherwise bound to do so. Burgess vs. Mendel, 62 Ala. 994.

**57. Mutual promises.** The exchange of mutual promises between parties to a contract constitutes a consideration. Such mutual promises may involve either, or both, of the previously mentioned elements, *i.e.*, benefit to promisor, or detriment to promisee.

EXAMPLE

Rich promised to act as a director of a bank and to deposit his money in the bank. In consideration of this, the bank promised to transfer to him a part of the stock in the bank. This was a valid contract. Rich vs. Lincoln State Nat'l Bank, 7 Neb. 201.

**58. An Apparent Consideration** may be unreal because,

1. It is impossible,
2. It represents only a moral obligation,
3. It is an act previously performed (a past consideration),
4. It is something that the doer was already bound to do regardless of the promise, or
5. It is illegal.

If any one of these five conditions exist there is no consideration, and the contract is unenforceable.

EXAMPLES

**Impossibility.** A agrees with B that if B will promise to pay him $500 he will go from New York to London in one day. This is impossible at the present time, and there is no consideration for the promise of B to pay $500.

**Moral obligation only.** Bates' brother was taken sick, while penniless and among strangers, who cared for him, and nursed him until he recovered. Bates afterwards promised to pay for the services, but the court said that Bates was not thereby obliged to pay, as there was no consideration, aside from a moral obligation.

**Past consideration.** Riley sold his farm to Stevenson, who paid the agreed price, and the bargain was fully completed. After the contract had been thus executed, Riley met Stevenson one day and said, "I will paint that house I sold you free of charge." Stevenson said, "I accept." This did not create a contract to paint the house, as there was no consideration for the promise to paint the house, the former contract to sell the house having been completed. Riley vs. Stevenson, 94 S.W. (Mo.) 781.

**Doing what one is already bound to do.** 1. Hatch secured a warrant which ordered Mann, the village constable, to arrest Gallup. This Mann refused to do unless Hatch would pay him five dollars. Hatch promised to

pay this amount, but after the arrest had been made refused to do so. The court said there was no consideration for this promise, because Mann was bound to make such arrests from the nature of his position. Hatch vs. Mann, 15 Wend. (N. Y.) 44.

2. If public officers perform services which would not ordinarily be required of them, they may recover on contracts offering them extra compensation for performing such services. See Reif vs. Paige, 55 Wis. 496, in which case the court held that a fireman was not bound to risk his own life to bring out dead bodies.

**Illegal consideration.** Cummings promised to buy liquor of a wholesale company, which agreed to sell it to him. The wholesale company, however, had no government license, and was prohibited by law from selling liquor. The company later sued Cummings because he refused to complete his contract and buy the liquor. The court said that he could not be compelled to do so, as the consideration was illegal. Perkins vs. Cummings, 2 Gray 258.

**59. Failure of Consideration.** If any of the conditions discussed in the preceding paragraph exist, there is no contract, because there was no consideration at any time. On the other hand, a contract may have been valid when it was made, but it may subsequently be invalidated by destruction of the consideration. This is called *failure of consideration*. Contracts in which the consideration totally fails after the contracts have been created, will not be enforced.

EXAMPLE

1. A contracted to sell to B a warehouse, which B promised to buy for an agreed price. After the contract was made, but before it was executed, the building was destroyed by accident, without the fault of either party. The court said that both of the parties were discharged from their obligations, because the consideration had failed. This contract was also impossible of performance. Powell vs. Dayton, 12 Ore. 488.

**60. Third Persons** may claim rights *because* of contracts made for their benefit, by other parties, even though they contributed no part of the consideration. It is first necessary for such a third person to show that the parties to the contract clearly intended to confer a personal right upon him. If the benefits are merely incidental to the main object of the contract, the third person cannot himself enforce the contract.

EXAMPLES

1. A loaned B a sum of money, in consideration of which B promised to pay the same amount on a future day to C, to whom A was indebted. C sued B on the contract, and the court said that there was a consideration for the

agreement between A and B, and that although C had contributed nothing to it, the contract was made for his benefit and he could recover. Lawrence vs. Fox, 20 N. Y. 268.

2. A water company contracted to supply a city with water for public purposes, including fire protection. Davis lost his house by fire, because the water supply failed, and sued the water company for his loss. The court said he could not recover on this contract against the water company, since the contract was not made for his benefit, which was merely incidental to the main object of the contract. Davis vs. Clinton Water Works, 54 Ia. 59.

**61. Options.** In the preceding chapter it was stated that an offer could be revoked at any time before acceptance. If, however, an offer is made to be open a definite time and there is a consideration for keeping the offer open, the accepted offer becomes an *option* which cannot be revoked until the time stated has elapsed. Options have great business importance, because a man to whom an offer is made may wish time to consider and investigate it. He may not wish to spend his time and money investigating if the offeror can withdraw the offer at any time. He is, therefore, at liberty to ask the offeror to promise to leave the offer open and in force for a definite time, if he will pay a consideration to the offeror for this promise. An option is in itself a contract, and requires a consideration.

EXAMPLE

A, having a piece of real estate, offered it to B for $5000. B, wishing to investigate its value, paid ten dollars for a thirty-day option at that price. Before the thirty days had elapsed A had an opportunity to sell it to someone else at a higher figure and claimed that no contract existed between him and B. The court said there was a consideration for his promise to keep the offer open. Clarno vs. Grayson, 30 Ore. 111.

**62. Formal Contracts.** In discussing the subject of consideration the examples have all been instances of simple contracts. If the contract were under seal, we have already seen that at common law no consideration was required. A formal contract offered the only means of making a valid, enforceable contract to make a gift to another. The rule has been changed by many states* so that the presence of a seal is only *presumptive evidence* of a consideration, and if it can be shown that nothing of value

* California, Illinois, Iowa, Indiana, Kentucky, Kansas, Massachusetts, Wisconsin.

was given, the contract may be set aside.* Other states have by statute abolished seals altogether, and the same rule applies where they are used that applies to simple contracts. In other states sealed instruments, with their quality of needing no consideration, are retained for contracts for the sale and transfer of real estate.

### EXAMPLES

1. A contract under seal stated that the sum of one dollar had been paid by one party to the other as a consideration. It was shown that this amount had never been paid. The court said that the contract could nevertheless be enforced because of the seal. Southern Bell Telephone Company vs. Harris, 117 Ga. 1001.

*Note.*— In states where a seal is merely presumptive evidence of a consideration the facts in the above case would destroy the contract.

## PRACTICAL SUGGESTIONS

In making a contract, assure yourself that there is a valuable consideration, *because* otherwise it will not be enforced.

Don't agree to do illegal acts, *because* your duty as a citizen directs you to uphold the law, not to break it.

Similarly, paying, or promising to pay, other persons for doing illegal acts is to be avoided, *because* you may lose your money, and certainly cannot compel them to perform their promises, which were invalid when made.

Don't make a contract which you think may require a seal, without consulting a lawyer, *because* only a lawyer can inform you as to the law of your particular state in this regard.

Insist upon paying something for another's promise to leave an offer open, *because* only then will it become an option; otherwise he may revoke it at his own pleasure.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1. Libbey promised to pay Eaton $100 for the privilege of naming Eaton's child. Eaton gave this privilege to Libbey, who named the child, but refused to pay the $100. Was there a contract? a consideration? Who received the benefit, if any? Who suffered the detriment, if any?

2. A city in July, 1862, adopted an ordinance, which it posted in prominent places, and in which it stated that it "hereby agreed to pay to every

* The difference between a formal contract and a simple contract, in the matter of consideration, is that in case of a formal contract consideration is always presumed until it is proved that there was none, while in a simple contract consideration is never presumed but must always be shown.

person who *had enlisted*, or who should *thereafter enlist* in the Civil War, the sum of $200." Frey had enlisted in May; Johnson enlisted in October. Can either collect the $200 from the city? Was there a contract? with whom? What was the consideration?

3. Bray was engaged to marry Bertha Snell. He promised to pay her $3000 if she would marry someone else. This she did, but Bray refused to pay her the $3000. Can she collect it? Was there a contract? a consideration?

4. Cowling believed himself indebted to Hicks for $5000, due a year later. Hamilton promised to pay this debt when it came due, if Cowling would give him (Hamilton) Cowling's house, and also agreed to pay Cowling $10,000 in cash. To this Cowling agreed and gave up his house to Hamilton, who paid him $10,000. Later it developed that Cowling had owed Hicks nothing. Can Hicks collect the $5000 from Hamilton? Why? Who furnished the consideration, if any?

5. A's property was on fire, and he promised the chief of the fire department $1,000 if he would do his utmost to put it out. He also offered him another $1,000 if he would rescue a child on the top floor of the burning building. The chief did both these things and attempted to collect $2,000. A claimed that both his promises were without consideration. Was any contract created? What? What was the consideration?

6. Woods wrote to Marks as follows:

"Chicago, September 1, 1915.

"I, Harry Woods, offer to sell you 60,000 bushels of spring wheat at 85 cents per bushel, delivered. Harry Woods."

Later and on September 3 he added the following:

"In consideration of $60, the receipt of which I acknowledge, I promise to leave the above offer open for acceptance until the hour of 1:15 P. M. September 14, 1915. Harry Woods."

Marks wrote accepting this offer September 13 and was informed by Woods that he had sold all his wheat. Was a contract created? Why? What was Woods' second writing called? Why?

## CHAPTER VII

## SUBJECT MATTER

All Subject Matter is Valid Except:

1. Against Public Policy
   - a. In restraint of trade
   - b. In restraint of marriage
   - c. Obstructive of Public Justice
2. Immoral
3. Fraudulent
4. Forbidden by Law
5. Criminal

Subject Matter

1. Form
   - a. An Act
   - b. A Promise
   - c. Property
2. Quality Must Be
   - a. Definite
   - b. Valuable
   - c. Legal

**63. Subject Matter** is that which forms the basis of the agreement, and about which the agreement is made. It has already been stated that this must be something lawful, possible, and definite in its nature, and may be the performance of an act, a promise, the surrender of a right, or the delivery of anything which the parties deem to have value.

**64. Prohibited Subject Matter.** Parties to contracts may agree to do, or not to do, any act not in the nature of things impossible and which is sufficiently definite to enable the courts to determine their intention, unless they attempt to create contracts which are,

1. Against public policy,
2. Immoral,
3. Fraudulent,
4. Forbidden by law, or,
5. Criminal.

If the subject-matter possesses any of these five elements, the attempted contract will be invalid.

**65. Against Public Policy.** The courts will not enforce contracts which are against public policy. Courts seek to promote the best interests of the public and will not lend their assistance to those who attempt to injure public welfare. A contract is against public policy if it is,

1. In general restraint of trade,
2. In restraint of marriage, or,
3. Obstructive of public justice.

These are the most frequently occurring kinds of contracts against public policy, though many others exist.

**66. Restraint of trade.** Contracts in general restraint of trade prevent free and natural competition. Such contracts tend to raise prices and are detrimental to the public at large. The right of buyers and sellers to compete freely in their business is a right which the law has always recognized.

An agreement may be in restraint of trade if it unduly limits a person in the time, place, or manner in which he may exercise his right to engage in free competition. Whether the restraint is undue depends upon the entire circumstances of each case.

EXAMPLES

1. Kingsbury contracted not to engage in the newspaper business in a certain town for five years. He made this contract with the purchaser of his newspaper. This contract was valid, and the restraint was not undue, but reasonable and valid. Andrews vs. Kingsbury, 212 Ill. 97.

*Note.*— On the other hand, a contract by which Ames agrees never to engage in the grocery business, or one in which Bates agrees not to sell lead-pencils at retail anywhere in the United States, can serve no useful purpose, and unduly limits the activity of Ames or Bates.

2. A, B, C, and D, all manufacturers of a useful commodity, combined in an agreement not to sell their product below a specified price, and only to sell a limited quantity each year. This agreement was against public policy and could not be enforced. Cummings vs. Union Blue Stone Co., 164 N. Y. 401.

**67. Restraint of Marriage.** Persons who make contracts by which they agree to prevent others from marrying, are interfering with a relation that is necessary to the best interests of society. Such contracts are void as against public policy.

1. Ames, Bates, Smith, Robinson, and Jones agree in consideration of the exchange of mutual promises that they will never marry. This contract is void and any party may marry at will without breaking a contract.

2. Palmer agreed with his wife that if she would bring suit against him for divorce, he would not contest it, and would give her $5000. The wife in accordance with this offer, and relying upon it, sued for divorce. The court refused to grant the divorce or to hear anything about the case, because the parties were acting upon a contract which sought to destroy the marriage relation. Palmer vs. Palmer, 72 Pac. (Utah) 3.

**68. Obstructive of public justice.** Persons who make contracts by which they attempt to interfere with public duties, public officers, or the administration of public laws, tend to corrupt our form of government. Such contracts are void, even though the particular act may have done the public no actual injury.

EXAMPLES

1. Schneider based a suit against a labor organization upon a contract in which the parties had for a sum of money agreed to use their influence to secure the appointment of a certain person to a public office. The court refused to hear the case, regardless of whether the person supported would have made a proper public officer. Schneider vs. Local Union No. 60, 116 La. 670.

2. Innes, a postmaster, agreed to locate the post-office in a certain building in consideration of a merchant's promise to pay part of the rent. This was illegal, as it tended to injure the public service, by interfering with the free discretion of a public officer. He should have placed the post-office where it would have been most convenient for the postal service. Woodman vs. Innes, 47 Kan. 26.

**69. Immoral.** Persons who attempt to make contracts in their nature immoral fail to create any binding legal relation, and such contracts are void.

EXAMPLE

A doctor agreed with Bates that he would represent that certain injuries which Bates had received in a railroad accident were of a serious nature, and that his compensation for medical services should be determined by the amount of the settlement which Bates secured from the railroad. This agreement was contrary to good morals in that it promoted dishonesty and lying. It created no contract. Jerome vs. Bigelow, 66 Ill. 452.

**70. Fraudulent.** If a contract is induced, or brought into existence, by fraud, the agreement is not void, but voidable, at the option of the party injured. (See Sec. 22.)

EXAMPLE

Stone employed Hardy to sell his farm, Hardy to receive a commission of one per cent of the selling price. Grant applied to Hardy for a farm, and

Hardy told him that he worked only for buyers of farms and that they paid his commissions. Grant then agreed to pay him $300 if he found a suitable farm. Hardy then introduced Stone and Grant who made a contract for the farm. Hardy sued Grant for his commission of $300, but the court said that he had secured the agreement with Grant by fraud, and that an agent of this kind cannot work for both parties. Grant vs. Hardy, 33 Wis. 668.

**71. Forbidden by Law.** A contract to do that which the law forbids will not be held good. Were the law to enforce such contracts it would be lending its aid to its own violation.

EXAMPLES

1. A made a contract to sell real estate to B, who agreed to buy. The contract was made on Sunday, and when A later refused to sell the real estate, B sued him on this contract. The court said that the contract was unenforceable in Indiana, because made on Sunday. Love vs. Wells, 25 Ind. 503.

*Note.*— Contracts made on Sunday are binding unless especially forbidden by statute. In a few states such contracts are void, in others voidable.

2. A promised to pay B $500 if he lost a bet which he made with B. He lost the bet, but the court refused to let B collect the money, because gambling contracts were prohibited by Pennsylvania law. State vs. Wilson, 84 Pa. 737.

3. A ordered B, a stock-broker, to sell wheat "on margins" for future delivery, his intention being simply to speculate and not to buy the grain, a fact which was known to B. B sued for his commissions as a broker, but the court said that B was a party to a gambling transaction and could not recover. Irwin vs. Williar, 110 U. S. 499.

**72. Criminal.** Persons cannot commit crimes without laying themselves open to punishment. Neither can they contract with other persons to commit criminal acts. By attempting so to do, they may themselves violate the law and become liable criminally. Thus one cannot agree with another to pay him for committing perjury (falsifying on the witness stand), forgery, robbery, burglary, or any act which the law has declared is a crime.

PRACTICAL SUGGESTIONS

It is unwise to contract regarding subject matter which you cannot describe accurately, *because* the courts will probably have the same difficulty and may declare it void for uncertainty

If you buy another man's business and good will it is poor policy to require him to unduly restrict his right to compete with you in the future, *because* you may thereby unlawfully restrain him, and if you do he can, if he wishes, open up a rival business next door.

Don't indulge in sharp practices and try to deceive another person with whom you are contracting, *because* the contract may be binding on you alone.

Comply with the state laws regarding licenses, if you are a physician, insurance agent, stock-broker, peddler, real estate agent, or are engaged in any vocation where a license is required, *because* you may later find that you have been working for nothing.

Avoid gambling contracts, not only because they are discountenanced by men of business integrity, but also *because* they are illegal and void.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1. Barber sued Alcott for services rendered as a physician at Alcott's request. It appeared that Barber was not licensed by the state board of health as required by statute in his state before a person could practice medicine. Can Barber recover for his services? Was there a contract? Why?

2. Gray and Hook were both applicants for the position of inspector of flour for the city of New York, a public office, the officer to be appointed by the governor of the state. Hook withdrew in favor of Gray in consideration of Gray's promise to pay him one-half the salary if appointed. Gray was appointed to the position, but refused to pay Hook anything. Can Hook recover from him? Was there a contract? Why?

3. Nunnemacher owned a single horse and wagon in which he delivered oil, which he sold at retail, in the city of Hammond. He sold his business to an oil company and agreed as a part of the contract of sale never again to sell oil in the state of Indiana. Later he sold oil in Hammond. Can the company with which he made the agreement recover from him? Why?

4. Perry invented a sand-papering machine. He sold his rights to a company and agreed for a consideration that he would never "manufacture, sell, or cause to be sold any sand-papering machines of any description." Later he invented a different type of sand-papering machine which he offered for sale. The company sued him to make him comply with his contract with them. Could they enforce compliance? Why?

5. (*a*) Jones, an unlicensed liquor dealer, delivered beer to Smith, who promised to pay for it. (*b*) Ames sold Bates grass seed, telling him that it was clover seed, though Ames knew at the time that it was not; and Bates promised to pay for it. Neither Smith nor Bates paid in the above examples. Jones and Ames sued them, respectively. Can they recover in either case? Why?

## CHAPTER VIII

## DISCHARGE OF CONTRACTS

- I. By Performance of all Conditions which may be
  - 1. Precedent
  - 2. Concurrent
  - 3. Subsequent
- II. By Intervention of Impossibility
- III. By Agreement
  - 1. Waiver
  - 2. Novation
  - 3. Modified Agreement
- IV. By Operation of Law
  - 1. Alteration of Instrument
  - 2. Merger
  - 3. Bankruptcy
  - 4. Death
- V. By Breach

**73. In General.** When two or more competent persons contract, we have seen that they thereby create rights on the part of one, and duties on the part of the other, which have not existed before. One party has a duty to do something which the other party has a right to demand; or each party may have both a right against and a duty toward the other. How can the contract be discharged and the parties freed from the obligations which they imposed upon themselves?

**74. Discharge by Performance.** The simplest manner in which a party to a contract can discharge his part of the obligation is to perform completely all that he agreed to do. When he has performed what he has agreed to do he is freed from further liability. He then has the right to compel the other party to perform his duties, if any, or to pay damages if he refuses to do so. Nothing short of a complete performance, in strict accordance with the terms of the contract, will operate as a discharge by performance.

EXAMPLES

1. A agreed to build a barn for B for the sum of $500. A performed his work, and B gave him $500. The contractual relation was discharged by the

performance of the respective agreements. McGuire vs. Neils Lumber Co. 97 Minn. 293.

2. If in the above example A had built the barn, and B refused to pay the $500, A alone would have been discharged and he could then have sued B for his part of the contract. Allen vs. Cooper, 22 Mo. 136.

**75. Conditions in contracts.** It was stated at the end of the preceding paragraph that every *condition*, which the contract imposed upon him, must be performed by a party before he will be discharged. Conditions in contracts are classified according to the period of time at which they should have been performed, into (1) precedent conditions, (2) concurrent conditions, and (3) subsequent conditions.

**A precedent condition** is a condition, imposed by the contract, which one party must perform before the other party is under any obligation to perform his part of the contract. It may also be a condition required to be performed before any contract exists.

**A concurrent condition** is a condition which must be performed by one party, at the same moment of time that he requires performance, by the other party, of some other condition of the same contract. Unless he performs or offers to perform the condition imposed upon him at the time he makes a demand for performance upon the other party, his demand is incomplete, and the other party is not in default as to his share.

**A subsequent condition** is the occurrence of some fact which the parties to a contract have expressly agreed shall destroy the contract in the event that it happens. The existence of a condition subsequent is a matter of defense. It must be proved to the court by the party who seeks to show that thereby the contract was discharged.

EXAMPLES

**Condition precedent.** A subscription was made to the stock of a corporation, to be due only when two hundred thousand dollars should be subscribed and a branch office of the company had been located in New York City. The total amount was subsequently subscribed, but no branch office was opened in New York City. The court declared that both these conditions must have been performed before the corporation had discharged its obligation and before it could collect from the subscribers. Brewer's Fire Insurance Company vs. Burger, 10 Hun. (N. Y.) 56.

**Condition concurrent.** Smith agreed in writing to convey 100 acres of land to Fuller, in consideration of Fuller's promise to pay him $6000.00

therefor. The payment of the money and the transfer of the land are conditions concurrent and neither party can compel performance by the other, or sue for damages, without showing that (1) he had performed his condition concurrent, or (2) that he had offered to perform it and his offer (called a tender of performance) had been refused. Fuller vs. Hubbard, 6 Cowen (N. Y.) 13.

**Condition subsequent.** If A sells a cow to B as a Jersey cow for $100 and agrees that B may return the cow if she is not a Jersey, the fact that the cow is not a Jersey is a condition subsequent, which entitles B to return the cow, receive his money, and be discharged under the contract.

**76. Substantial Performance of Conditions.** Nothing less than a complete performance of all the conditions of a contract, with strict adherence to their terms, will operate as such a discharge of one party as to entitle him to compel performance by the other party. A court of equity will sometimes, in cases of great hardship, allow a party who has substantially performed his part to recover the value of his partial performance, and discharge him under the contract. An exception to this rigid rule of the law courts exists in contracts to do complicated and expensive things, in cases in which the deviation from the expressed conditions may be slight.

EXAMPLES

1. Brown, a tailor, agreed to make a suit of clothes for Foster to his entire satisfaction. Foster was not pleased with the suit and refused it. Brown sued for the price, and proved that the clothes were well made, barring a slight defect, which could have been easily remedied. The court refused to allow him to recover, however, as he had not performed his condition, which was to satisfy Foster. Brown vs. Foster, 113 Mass. 136.

2. In the United States the substantial performance of a building contract, if the deviation was made in good faith, permits recovery. In such a contract, slight omissions or defects are likely to occur through some excusable oversight, inadvertence, or mistake, in spite of the most honest and intelligent efforts to perform in every particular. "To hold that the builder could not, in such a case, recover on his contract, would be too rigid a rule to apply to the practical affairs of life." Leeds vs. Little, 42 Minn. 414.

The entire contract price of a building was $2500, and damage by defective construction, together with the amount necessary to repair the defects, amounted in value to $876. The court said this did not constitute a substantial performance within the above rule. Ketchum vs. Herrington, 45 N. Y. S. R. 59.

**77. Time of Performing Conditions.** The conditions in contracts must be performed within a reasonable time, if the

contract itself specifies no date for performance. On the other hand, if the parties specify in their contract a date for its performance, time is said "to be made part of the essence of the contract," and the condition must be performed on that date, in order to entitle a party to be discharged thereby. What constitutes a reasonable time, when no date is specified, depends on the nature of the contract and all the circumstances of the case. Similarly, express provisions as to time are construed by the courts in the same way as persons of ordinary intelligence would construe them. Fractions of days are not noticed by the courts, unless the parties specify that they should be. If the date of performance is placed on Sunday, the parties are allowed until Monday.

EXAMPLE

Shinn contracted to sell a farm to Roberts, who agreed to buy it for $117 an acre. The contract was in writing and stated that the deed to the farm should be delivered at a specific bank on March 20 at ten A. M., when Roberts was to pay his money. Roberts was at the bank ready to pay at the hour named, but Shinn did not appear until five o'clock, when he offered the deed to Roberts, who refused to take it. Shinn then resold the farm for $99 an acre and sued Roberts for the difference as the damages which he claimed Roberts had caused him. The court declared that Shinn could not recover his loss from Roberts because he had not performed the condition imposed upon him as to the time required. Shinn vs. Roberts, 20 N. J. L. 435.

Note that the above contract was a contract to sell, not a sale.

**78. Payment.** Payment may be in money, or in the delivery of property or rights, according to the contract of the parties.

**Tender.** A tender is an offer to pay. A penalty for nonpayment may be avoided by an actual transfer of the thing to be paid or by a tender of payment.

EXAMPLE

Hayden contracted to sell and deliver to Demets 50,000 pounds of copper of a specified quality, to be paid for in thirty days. Copper of the specified quality and weight was unloaded on Demets' platform, but he refused to accept it. Hayden took the copper to his warehouse, and notified Demets that he would hold it subject to his order. At the end of thirty days he sued Demets for the agreed price and the court allowed him to recover. Hayden vs. Demets, 53 N. Y. 431.

Payment and tender are matters of defense. The party who claims to have paid or to have tendered payment must prove this in court. To prove that a tender has been properly made, a

party must show that he made an unconditional offer to perform the condition at the proper time and that the other party refused to accept the money or other thing offered; and he must hold himself still willing to perform, except in so far as the wrongful act of the other party has injured him or placed him in such a position that he can no longer do so.

**Legal Tender.** If the tender be of money the party who made the tender must also show that he offered to pay money which the law declares is "legal tender," and that he actually produced such money and offered it to the other party. An offer of payment by means of money that is not legal tender is sufficient, unless the other party specifically objects on the ground that the money offered is not legal tender money.

**Legal tender money.** Congress has provided that the following moneys shall be legal tender: (1) Gold coin and silver dollars in any amount; (2) silver coins, less than one dollar, in amounts not exceeding ten dollars; (3) copper and nickel coins up to twenty-five cents; (4) greenbacks for any amount, except for duties and interest on the public debt; (5) treasury notes in any amount, except for duties and interest on the public debt. Bank notes are not legal tender.

**Effect of tender.** The effect of a tender is to relieve the one who makes the tender from liability for interest on the debt from the time of the offer and from the liability for court costs in case the court decides that the amount offered was sufficient. This does not in any sense discharge the debt.

**79. Intervention of Impossibility.** Contracts to do things that are by their nature impossible are void from the beginning, as previously stated. Sometimes, however, a contract that at the time of making seemed possible, becomes impossible by operation of law or the destruction of the subject matter.

EXAMPLES

1. A contracted to make repairs on Bates' house, which was destroyed by fire the day after the contract was made. The court said that both parties were excused from performing this contract, because it could only be performed if the house remained in existence. Butterfield vs. Byron, 153 Mass. 517.

2. A conveyed land to B, who contracted that he would build a row of flat buildings on it. The city, however, condemned the property by proper

legal proceedings and built a city hall on it. B was discharged from further performance of his contract with A, because of the act of law. Baker vs. Johnson, 42 N. Y. 126.

3. A famous opera singer contracted to sing in a concert in Boston for a specified two weeks' engagement. Before the date set she became critically ill, and failed to appear. When the manager of the opera house sued her for violating her contract, the court declared that her illness excused her from performing the contract, and said that contracts for personal service are always made subject to an implied condition that the party shall be alive and physically able to perform. Marvel vs. Phillips, 162 Mass. 399.

¶ 80. **Discharge by Agreement.** Not only may the contract be discharged by performance, and in some special instances by impossibility of performance, but the parties to a contract may mutually agree that it shall be discharged. If they so agree the law will give effect to their intention, and all obligations under the original contract thereby cease to exist. Their agreement to discharge the contract, which is itself of the nature of a new contract, may take one of three different forms. It may be either (1) a waiver, (2) a novation, or (3) a modified agreement.

**A waiver** is the mutual relinquishment of all rights which were created by the contract. In executory contracts the consideration to support this new agreement is found in the mutual promises of the parties. In contracts executed by one party a valid waiver can be made only upon a valuable consideration, or by a contract under seal. The term *waiver* is also used to indicate the relinquishment by one party of any of his rights.

**A novation** is the discharge of one of the parties by substituting in his place some other person, not originally bound by the contract. A novation can be accomplished only by agreement of all the parties to the contract.

**A modified agreement** consists in the substitution of some new contract for the one which previously existed between the parties. When made, the new agreement, and not the original one, determines the rights and duties of the parties.

EXAMPLES

1. Ames agrees to employ Bates as a stenographer at the salary of fifty dollars a month, and Bates accepts. Later Ames employs another stenographer and Bates secures other employment. Both agree to cancel their contract. This discharges both parties.

2. Paine owed Doe $100, and Doe owed Foster $100. The three parties met and agreed that Paine should pay Foster $100. As a consideration for this agreement Doe promised to release Paine and Foster promised to release Doe. Later, Paine refused to pay Foster, and the court said that the novation destroyed the original contract and allowed Foster to recover from Paine. Foster vs. Paine, 63 Iowa 85.

3. Taylor made a contract to build a rosewood cabinet for Pulliam for the sum of $100. He was unable to secure any rosewood, and offered to furnish Pulliam other specified furniture instead. Pulliam accepted and the other furniture was delivered to him, but he refused to pay the price. The court said he must do so, and declared that the original contract to deliver a rosewood cabinet had been discharged. Pulliam vs. Taylor, 50 Miss. 251.

**81. Discharge by Operation of Law.** One or both parties to a contract may be discharged from their obligations because of changed conditions, or because of acts on their part, other than performance, which the law expressly declares shall discharge the contract. These may be either (1) wrongful alteration of a written instrument, (2) creation of a merger, (3) becoming bankrupt, or (4) death.

**82. Alteration of instrument.** If a deed or any simple contract in writing be wrongfully altered by an addition, interlineation, or erasure, by one of the parties, the other party to the contract is thereby released from further obligation. This rigid rule of law was adopted to prevent parties from tampering with the written evidence of their contracts.

EXAMPLE

Clark, by a written contract promised to pay McGrath $100 on April first, with interest at the rate of five per cent. McGrath changed the rate of interest to six per cent. He later sued Clark on this contract, and the court said that he could not recover, because he had altered the contract. McGrath vs. Clark, 56 N. Y. 34.

**83. Merger.** A contract is discharged if its terms are included in another contract of higher legal value. This can take place when the terms of a simple contract are included in a contract under seal. If this is done the simple contract is discharged, for it is supplanted by the sealed contract. Similarly, an open account may be merged in a judgment based upon it.

EXAMPLE

Myers agreed orally to transfer stock in a corporation to Hewitt, who agreed to buy it. Later they made a similar agreement to the same effect

under seal. Thereafter the rights and duties existing between them were determined by the contract under seal and not by their original agreement. Myers vs. Hewitt, 16 Ohio 453.

**84. Bankruptcy** is a third condition under which the law will discharge the rights and duties of parties to contracts. Bankruptcy is a proceeding by means of which all of a person's property is divided among those whom he owes, called his creditors, after which all his liabilities, on contract and otherwise, are discharged.

It often happens in business that a man becomes hopelessly involved with self-imposed duties and liabilities. If he were to continue through life with this burden, he could improve his own condition only in rare instances, and might become a drag on society. The law has therefore said to him, "If you will turn over all your property to the Federal court to distribute among your creditors, you may become discharged from your debts, and start anew."

Or it may happen that his creditors believe him to be unable to pay all of them, or discover that he is trying to pay part of them at the expense of the rest, or that he is trying to conceal his property to defraud them. If so, the law declares that they may, through the medium of a Federal court, have his property divided among them, but provides further that if they do so they must discharge him from all his duties and liabilities.

It is customary to call any person who is in financial difficulties, a bankrupt. This is not a correct use of the term, for no person is a legal bankrupt until one of the Federal courts of the United States has declared him so.

If a person wishes to secure a discharge of his debts in a bankruptcy court he first files a petition asking that the court declare him to be a bankrupt.

If he pursues this course and becomes a bankrupt of his own will and act he is called a *voluntary* bankrupt.

If the creditors of a man desire to have his property divided, they file a petition with the court. They must show, however, that he is insolvent and that he has committed what is called an act of bankruptcy. Such an act may be that he has preferred some of his creditors to others while insolvent, or that he has dealt with his property so as to defraud creditors, or has consented in writing to be declared a bankrupt.

When the bankruptcy proceedings are brought by the creditors, the debtor is called an *involuntary* bankrupt.

If the court declares the debtor a bankrupt, it also appoints some person to be *receiver* of his property. The bankrupt files a list, or schedule, of all his property and all his debts. The

receiver collects all the money, and other properties, belonging to the debtor, which he can find, reduces all to cash, and holds the proceeds for division among the creditors who have filed claims with the court. The debtor, however, is entitled to keep certain things, called his *exemptions*. These are usually his home, and his furniture and similar articles. What these are depend on the state law.

If the bankrupt has acted fairly throughout all these proceedings; if he has actually surrendered all his property; has not been declared a voluntary bankrupt then within six years preceding and prior to bankruptcy did not obtain credit by a materially false statement in writing; he will be entitled to petition for a discharge. If the court grants his petition he will then be discharged of all his old debts, and may begin his business career anew, untroubled by old liabilities, unless he wishes to renew them expressly by a new promise to pay.*

**85. By death.** The only classes of contracts discharged by death are executory contracts for personal services, in which personal skill and taste are involved, or personal trust and confidence between the parties. If these conditions are present, the death of one of the parties discharges the contract. But in contracts which do not involve these elements, and which can be as well performed by another, the contract is not discharged by the death of one of the parties, and may be enforced against his estate. The effect of the death of a joint contractor has been discussed. (See Sec. 27.)

## PRACTICAL SUGGESTIONS

Respect the conditions imposed upon you by a contract, *because* otherwise you may thereby become disabled to demand performance by the other party.

* All debts, on contract or otherwise, may be discharged by a court of bankruptcy, except: (1) taxes levied by the United States, state, county, district, or city in which he lives; (2) judgments in actions for fraud, or obtaining money by false pretenses or false representations, or for willful and malicious injuries to the person or properties of another; (3) alimony or maintenance of his wife and children as decreed by a court; (4) claims which were not duly included by him in his schedule in time for proof and allowance, unless the creditor knew of the proceedings, or, (5) debts which were created by his fraud, embezzlement, misappropriation, or defalcation while acting as an officer in a capacity of trust.

Perform the conditions imposed upon you at the proper time, *because* you have given the other party the right to expect that you will do as you agreed, and if he is disappointed he will probably sue you.

The alteration of written contracts without the consent of all parties is perilous and the law is drastic and severe as to such offenses.

Don't transact business with anyone in danger of bankruptcy, *because*, no matter how much he may wish to prefer you to his other creditors, it is the purpose of the bankruptcy law to treat all creditors alike.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1. On February 2, 1914, Pope in New York agreed to sell and Hager in St. Louis to buy 300 tons of No. 1 Iron at a specified price. On January 8, 1915 the iron arrived in St. Louis and Pope offered to deliver it, but Hager refused to accept it. Pope then sued Hager for the agreed price, proving a tender on his part of the iron. Can he recover the price from Hager? Why?

2. The following is a copy of an agreement between two parties:

"For value received, I promise to pay or deliver to Catharine Corbitt. $100 in such articles of merchandise, and at such times, as she may select.

(Signed) L. Stonmetz.

Accepted, Catharine Corbitt."

Later Miss Corbitt wrote the following to Stonmetz:

"I call upon you to perform your promise. Catharine Corbitt"; and he doing nothing further, she sued him. Was this proper without any further act on her part? What conditions did the contract impose on each party?

3. Ames contracted to build a woodshed for Bates for an agreed price, promising to complete it before June first. When the woodshed was half built on May first, Ames fell from the roof, breaking his leg and further disabling himself. He then employed Call, without Bates' consent, to complete the woodshed, and when it was completed, which was before June first, he sued Bates for the agreed price. Was this a proper performance on his part? Why?

4. Jones went to Black, a tailor, for a suit of clothes to be made to order. He selected the cloth from Black's stock and said to Black, "If I am not perfectly satisfied with these clothes in every respect, after they are finished and I have tried them on, I will not take them." Black replied, "All right." After the suit was finished and Jones had tried it on he refused to keep it on the ground that one shoulder did not suit him. Black sued him for the price and proved by other tailors that the shoulder was an excellent "fit," and that no one could do any better on account of the fact that Jones had a broken collarbone which had been improperly set. Under all these circumstances could Jones properly refuse to take the suit? Why?

## DISCHARGE OF CONTRACTS — Continued

- I. As to Consequences
  - 1. Money Damages
    - a. Divisible Contracts
    - b. Breach of Subsidiary terms
  - 2. Discharge from further Performance
  - 3. Specific Performance
- II. As to Time
  - 1. Anticipatory Breach
  - 2. At Date of Performance

**86. Breach of Contract.** The fifth method by which one's obligation, or duty, created by a contract, may be discharged, is by a wrongful act of the other party. A wrongful act which discharges the innocent party to a contract may be either the failure of the other party to do something which by the contract he has agreed to do, or the act of the other party in doing something which by the contract he has agreed not to do. Such omissions or acts violate the terms of the contract, and are called *breaches* of the contract.

**87. Consequences of Breach.** When there has been a breach of contract, the injured party is entitled to either (1) money damages, (2) discharge of his own obligation to perform, or (3) the right to enforce performance. Which of these rights he is entitled to depends upon the circumstances and the law covering the particular case.

Whether the injured party is limited to damages, or whether he may also be excused from his own performance, depends on the nature of the terms which the other party has violated. The injured party will be discharged from the contract, in addition to having an action for damages, unless,

1. The contract is divisible, or,
2. The term which was violated was subsidiary to the main purpose of the contract.

**88. Divisible Contract.** A contract may consist of a number of promises to perform a series of acts, really a series of separate contracts. If this be true, the failure of one party to perform one of these acts does not discharge the other from the whole contract, or even entitle him to sue as for breach of the whole contract. A breach in such a contract operates only on that part of the contract which it affects, and no other. It is often difficult to determine whether a contract is entire or divisible, and each case must depend entirely upon its own facts. If, however, the contract be divisible, a breach gives rise only to an action for damages, and does not operate to discharge the contract.

EXAMPLES

1. Under a contract Norrington agreed to sell to Wright "5000 tons of iron rails, for shipment from a European port, or ports, at the rate of about 1000 tons per month, beginning February, 1880, but the whole contract to be shipped before August first, 1880." Norrington shipped in February 400 tons, which Wright received and paid for, but when Wright learned that only 885 tons had been shipped in March he refused to receive them and cancelled the whole contract. The court declared the contract to be entire, and said that the failure to ship 1000 tons a month was a breach of the entire agreement as that was what had been contemplated. Norrington vs. Wright, 115 U. S. 188.

2. Cahen sold to Platt 10,000 boxes of glass to be delivered during the months of October, November and December, to be paid for on delivery. Cahen delivered 4000 boxes in October which were not up to specifications agreed upon in the contract and Platt cancelled the whole agreement. The court, however, interpreted this as a divisible contract and declared that a breach only affected a part of the contract and did not permit of cancellation of the whole. Cahen vs. Platt, 69 N. Y. 348.

*Note.*— The two examples above may seem very similar, but it will be observed that in the first example Norrington's failure to ship 1000 tons a month had already violated a principal clause of the whole contract, while in the second example Cahen still had plenty of opportunity during November and December to fulfil his contract, even though the first shipment of 4000 boxes was unsatisfactory.

**89. Breach of Subsidiary Terms.** It would be grossly unfair to allow a party to refuse to proceed with a contract because the other had violated, perhaps unintentionally, some term which was of little vital importance. The law has recognized this and does not permit such a result to follow. If the term which is violated does not go to the essence of the contract, it

will merely give rise to an action for damages, but will not entitle the innocent party to cancel the entire agreement.

**90. Specific Performance.** Sometimes damages, which are always measured in money, will not compensate a person for the loss of benefit which he has suffered by reason of the violation of the terms of the contract by the other party. Such a condition often exists in case one has contracted to buy a house or farm, desiring, for some personal reason, to secure the particular house or farm for which he contracted. No other will satisfy him, and no amount of damages will entirely pay him for his loss. Recognizing this fact, courts of equity enable a party who has made a contract regarding real estate to compel the other party to do actually as he agreed. If he agreed to sell a farm, he will be compelled to convey it; and the rule works both ways, for the purchaser may be compelled to accept it and pay the price. This remedy is called *specific performance* and applies, with few exceptions, only to contracts for the sale and purchase of land. If, after one has been so ordered to perform his promise, he continues to refuse, the court of equity will declare him to be in contempt of court and order him punished.

In contracts to buy or sell personal property it rarely happens that money damages will not suffice as compensation, but in rare instances, as where one has agreed to sell another an heirloom, or a patent right, which can be purchased of him alone, the innocent party may secure a *decree of specific performance*, as it is called, of a contract to sell personal property.

EXAMPLES

1. Ames contracts to sell Blackacre to Bates for $5000, who agrees to accept it at that price, the contract being in writing. Later Ames refuses to perform his part. Bates makes a tender of the money, which is refused, and then sues Ames in a court of equity, which will, in the absence of fraud or mistake, order Ames to accept the money and convey the land.

2. Parker, a contractor engaged in building a court house, entered into a contract with Neal to buy 200,000 feet of pine boards to be cut from a specific tract of pine timber situated in Caroline county, known as the "Bennett Todd Tract." He desired this particular lumber in order to comply with the specifications for the court house, and no other lumber in the vicinity was satisfactory. When Neal broke the contract, the court declared that the circumstances were exceptional and would entitle Parker to have specific performance by Neal, even though it was a contract to sell personal property. Neal vs. Parker, 98 Md. 254.

**91. Anticipatory Breach.** Violations of a contract may occur before the time of performance. Ames, who has agreed to sell his house to Bates on the first of July, may have declared on the first of May that he repudiated his contract and refused to be bound by it, or he may have torn down his house. In either event, whether it be by express renunciation or by act, Ames is said to have committed an anticipatory breach of his contract, being a total violation of it before the time of performance. If such anticipatory breach be committed, the innocent party need not wait until the time of performance, holding himself always ready to perform his own part of the contract, but is at once discharged from his obligations, and may immediately sue the other party for his damages.

This is subject to the limitation that except in mutual promises to marry, or similar contracts calling for continued steadfastness, the party committing such an anticipatory breach may repent and withdraw his repudiation, even against the other's protest, at any time before it is acted upon by the innocent party or has caused him damages.

EXAMPLE

Clark employed Marsiglia to clean paintings from a picture gallery, but before the latter began the work Clark countermanded his directions and refused to continue the contract. Marsiglia, however, proceeded with the work and when it was completed sued Clark for the entire contract price. The court decided that he could only recover the expenses which he had suffered at the time Clark repudiated the contract and the profits on the whole contract. He had no right to continue the work. It was his duty to keep the damages as low as possible. Clark vs. Marsiglia, 1 Denio (N. Y.) 318.

**92. Damages for Breach of Contract.** If the injured and innocent party to a contract which has been broken, sues for damages, he may recover the amount of loss which he has suffered. This loss is estimated in money, and is measured by the net value of the contract, or what he would have realized had the contract been performed. The net value includes the actual outlay and the profits which could have been reasonably anticipated. Remote and uncertain, or speculative, damages cannot be recovered, but only those which can be readily computed and ascertained. If no anticipated profits be proved, the injured and innocent party may recover the net expenses which he incurred in preparing to perform his part of the contract.

The fundamental idea of the assessment of damages is that the party who has been injured by the other's breach of contract may recover for the loss of the *benefit* which he would have received had the contract been performed. This loss of benefit is measured by the difference in value between what he received and what he should have received.

No one can recover damages for breach of contract if he himself caused the breach to be committed. If one party contracts to build another a house by May first, from materials to be furnished by the latter, the party for whom the house was to be built cannot object because it is not completed within the time specified if he failed to furnish the materials promptly. "One cannot recover for his own wrong."

The assessment of damages for breach of contract is largely a matter of computation from the facts of the particular situation, the aim always being to determine the money value of specific losses and the money value of the loss of the *benefit* caused by the breach.

EXAMPLES

1. Deeds contracted to purchase from Gardner 500 buggies of specified description and at stipulated prices, to be ordered as needed. Gardner, relying on the contract, purchased all the necessary material and constituent parts, but Deeds repudiated the contract. Gardner sued for damages, without manufacturing the buggies, and was allowed to recover at once the profits which the contract would have yielded, in this case the difference between the contract price and the cost of production. Gardner vs. Deeds, 116 Tenn. 128.

2. Meech contracted to furnish a hall for the performance of a theatrical company, and to retain one-half the gross profits for the use of the hall. Later he refused to furnish the hall and the theatrical company sued him and attempted to recover an amount which they claimed would have been one-half the gross profits. This they could not do, because such profits were purely speculative and not susceptible of proof. The amount of their damages was limited to the expense which they had incurred preparing for the engagement. Bernstein vs. Meech, 130 N. Y. 354.

**93. Summary of Rights Caused by Breach.** (I) One who seeks to recover damages because of another's violation of the terms of a contract must show:

1. That he did not cause the breach of the other, and that the breach was of a condition precedent to any duty on his part, or,

2. That it was the breach of a condition concurrent, and that at the time and place of performance he was himself ready and willing to perform, or,

3. That it was an anticipatory breach, which he acted upon.

In each of the above cases he must show that he was thereby damaged in an amount capable of proof.

(II) One who seeks to cancel a contract because of another's breach cannot do so, if

1. His own promise was independent,
2. The contract was divisible, or
3. The term which was violated was subsidiary to the main purpose of the contract.

(III) One who seeks a decree of specific performance for breach by the other must show:

1. That he is ready and willing to perform his part,
2. That damages will not adequately compensate him for his loss.

## PRACTICAL SUGGESTIONS

Avoid making oral contracts to buy land, *because* if the price goes up the other party may decide to keep his land and you cannot ask the court to order specific performance of such an agreement.

A continuation of performance of your side of a contract after the other party has committed a total anticipatory breach is unnecessary and improvident, *because* you can only recover for the loss you suffered up to that time, not afterwards.

The performance of acts which may result in the other party committing a breach of his contract with you is dangerous, *because* you may thereby become the one at fault — both morally and legally.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1. Gregory agreed to work for Mallory for nine months at thirty dollars a month, payable at the end of his employment. Two weeks before the work was to begin, Mallory informed Gregory that he did not need him. What can Gregory do about this?

2. The White Sox, a Chicago baseball club, contracted with Whitney, a noted pitcher, agreeing to pay him $12,000 for the next season's playing, and Whitney accepted this agreement. Before the season opened he made a new contract with another club at a higher salary, and refused to play with the White Sox. What can the White Sox do about this?

3. Jordan employed Wright to renovate and cleanse the rugs and carpets of his hotel for a certain sum. Wright called for and obtained them

and took them to his place of business and began work upon them, but before he was half done Jordan told him he need not clean the others, as he was about to sell the hotel. As Wright had gone to the trouble to get them from the hotel and had been at expense in employing an assistant for the entire work, he went ahead and cleaned them all, and redelivered them to Jordan, who had not sold as he expected. Jordan refused to pay anything and Wright sued him. How much, if anything, can he collect?

4. By a valid contract Ames promised Bates to paint him a picture to be delivered at Bates' public gallery at a certain date. A month before that date Ames' arms were permanently paralyzed. Bates did his best to find some one else who could paint a suitable picture to take the place of Ames' work, but failed, Ames being the best artist in America. The agreed price for painting the picture was $4000, and on account of its absence the exhibition was a failure and Bates lost $3000. Bates sued Ames for $3000, and Ames sued Bates for $4000, claiming that it had become impossible for him to perform his conditions under the contract. Who is in the right? Why?

5. Morgan employed Moore to clean his sidewalks for the winter, promising to pay him $3.00 each time it was necessary to clean them. Moore cleaned them sixteen times and then secured a permanent position and refused to continue his work. It was necessary for Morgan to employ another man at $4.00 for each of ten additional cleanings, and he refused to pay Moore anything, claiming that Moore had broken his contract and that this excused him from any further performance on his part. Moore sued him for $64.00. Can he recover?

## CHAPTER X

### REMEDIES

**94. Purpose of Remedies.** It has long been the boast of our law that under it there is provided a redress for every wrong. The legal means which the law uses for this purpose are called its remedies. In case the wrong is a public one, it is called a crime, and its punishment is provided by the criminal law. Commercial law, however, is directed particularly to the rights and injuries of individuals arising out of contracts. The remedies provided for injuries to these rights are called *civil remedies*. These are always secured through the formality of "a suit at law," for it is a maxim of the law that "No man shall be condemned unheard," and that "Every man has his day in court."

**95. Legal Steps.** The following are the formal steps which make up "a suit at law," and enable a party who has been civilly wronged, whether by breach of contract or otherwise, to recover his damages:

1. Summons,
2. Pleadings,
3. Trial,
4. Judgment,
5. Execution,
6. Levy,
7. Sale.

**96. Summons.** The first step is to secure from the clerk of the court a summons,* and have it served upon the party whom one wishes to sue, called the *defendant in the action*. This summons gives the defendant notice of the commencement of the law-suit, and of the day, place, and hour of trial, that he may have the opportunity to be present and make his defense.

**97. Pleadings** are the written or oral statements of the parties, to the court, describing the nature of their claims. Copies are usually required to be furnished to the opponents so that they may know on what matters to prepare for the trial.

*In many states the clerk of court no longer issues the summons, but it is drawn up and signed by any lawyer, being deposited with the clerk of court only after it has been served on the defendant.

**98. The trial** is conducted by a regular and well understood code of rules, each party being allowed at the proper time to offer evidence in his own behalf. The person who began the law-suit is called the plaintiff, or complainant, and he must prove his side of the case by the weight of evidence. If the testimony appears to be balanced, the suit will be dismissed, for he who sues another must always prove his claim. Thus if the law-suit be one in which a debtor is made the defendant and the action be started to collect the debt, the trial begins with the presumption that the defendant owes nothing, and the plaintiff must overcome this presumption by producing more evidence to the effect that he does owe it than the defendant produces that he does not.

**99. Judgment.** If the case be heard by a jury its decision is called a "verdict." The verdict, when "entered" upon the records of the court is called a judgment. The judgment varies according to the relief sought. It is generally expressed in terms of money, since money is usually the best measure of damages for a wrong. When a judgment is entered by a *court of record** it usually becomes a lien on the real estate owned by the defendant within the county. This means merely that the plaintiff can collect his claim out of the real estate, if the defendant refuses to pay him in money, and that it makes no difference even if the defendant sells the real estate, because the judgment continues to be a lien upon all the real estate which the defendant owned in the county when it was rendered, until it is paid.

When the judgment is rendered the legal steps have proved of little actual satisfaction to the plaintiff, for the debtor still owes him and he has merely substituted the judgment for the original evidence of the debt. The law, however, provides a manner in which a judgment can be collected, provided the debtor has any property not exempt. (See table of exemptions in appendix.) This step is not applicable except when the debt has been reduced to a judgment, for only by following the three preliminary legal steps can it be fully determined that no injustice is being done and that the debtor actually owes the debt.

* *Courts of record* are those whose acts and judicial proceedings are required by law to be enrolled and preserved for a perpetual memorial. Inferior courts such as justice courts, and in some states, municipal or city courts, are not courts of record.

At the point where judgment is rendered the steps taken have been to fix the liability with certainty; the remaining steps are provided as a means of realizing upon that established liability.

**100. Execution.** This is an order issued by the court to its executive officer (constable or sheriff), directing him to seize the property of the debtor and convert it into cash, that the judgment may be paid. The execution is usually first served upon the debtor, by reading it to him, with a demand made upon him by the officer for either cash or property with which to satisfy it.

**101. Levy.** In case the debtor refuses or neglects to turn over property in satisfaction of the execution when it is served upon him, the officer may seize any property, not exempt, that he may find belonging to the debtor. This is called "making a levy." Property so seized is, after being advertised according to law, exposed for sale, usually at auction to the highest bidder. The proceeds are first applied in satisfaction of the costs and expenses of the suit and of the levy, then to the claim itself, after which, anything remaining is turned back to the debtor.

**102. Exemptions.** Not all property owned by the debtor is subject to levy under an execution. The several states have passed statutes called "exemption laws," by the terms of which a debtor may, in any event, retain certain of his property. This is to prevent the individual from being deprived of the necessities of life, or of the resources by which these necessities may be obtained, so as to be in danger of becoming a public charge. As a rule, the heads of families are the most favored class in this regard. The exemption laws are entirely a matter of statutory regulation, and the student should consult the statutes of his own state for further details. (See appendix.)

**103. Garnishment.** The debtor may have no property subject to execution, but it may be that a third person owes him on account, on a note or in some other form of indebtedness. This person is called in and made to testify as to the amount of the indebtedness. A judgment is then rendered against him for such amount as may be due, in favor of the plaintiff. This is called "garnisheeing the debt of another."

It is also possible to employ this means of collection at the commencement of the original law-suit, in order to prevent the person to be garnished from paying the defendant while the law-suit is in progress.

Government, municipal, and other public employees are not subject to garnishment of their salaries.

**104. Replevin.** When a party fails to perform that which he contracted to do, the law, as we have seen, gives to the injured party a redress, which is, in nearly all cases, a *money damage*. The law does not usually compel a party to perform his contract literally, neither can he, as a rule, be imprisoned for not doing so. There are cases, however, when the law does not deem a money compensation a just equivalent for the wrong suffered. One of these is a case in which the defendant unlawfully takes and detains the goods of another. The remedy for this wrong is called *replevin*. The executive officer of the court takes possession of the goods, by virtue of a statement of authority issued by the court called a *writ of replevin*, and if after the trial the judgment is in favor of the plaintiff, the actual goods are delivered to him; but if in favor of the defendant, the goods are returned to him. The scope of this action has been generally much enlarged by statute, until now it embraces all cases where the property of another is unlawfully *detained*, regardless of whether the original taking was lawful. It is certainly, where applicable, a wholesome remedy, and without it the law would in many cases fall far short of giving complete redress.

**105. Attachment.** Before the plaintiff could go through the long formalities of a suit at law, obtain a judgment, and secure an execution, the defendant might, if he desired to do so, put all his property out of his hands, or perhaps flee from the state. In such cases the court will issue an *attachment*. This is in effect reversing the order of the steps, bringing the execution first, after which comes the trial, judgment, etc. A suit can be commenced by means of an attachment only when the plaintiff will state on oath before the court that the debtor is planning to flee from the state, has disposed of or threatens to dispose of his property, or in some other manner, specified by statute, has acted or threatens to act in such manner as to make

the plaintiff's judgment uncollectible, unless the debtor's property be seized immediately. It is a grave thing to deprive a man of his property before it is legally determined that he is indebted to the plaintiff, and in most states the court will not issue a *writ of attachment*, ordering the executive officer to seize the goods, unless a bond is filed with the court, by which the plaintiff agrees that he and his bondsmen will pay the defendant for all the damage he has suffered, if it should finally be determined that he did not have a right to the writ of attachment.

**106. Injunction.** This is called a negative remedy. It is designed to prevent a prospective injury rather than to give redress for a wrong already committed. If a person can prove to the court that some other person is about to do that which would be an irreparable injury to him, for which money damages would be an inadequate remedy, he can secure an *injunction* against the wrong-doer. This is the order of the court which informs the wrong-doer that he must not commit his threatened act, and restrains him from committing it. If he persists he will then violate the injunction and will be said to be "in contempt of court," for which contempt the court will fine or imprison him. Ordinarily one cannot secure an injunction to prevent another from breaking his contract.

**107. Specific Performance.** This remedy has been previously mentioned. It is a remedy which consists in the decision of the court that the defendant shall do the particular act which he agreed to do. It has already been stated that this remedy is applicable in only a few well defined cases, usually being confined to contracts for the sale or purchase of real estate.

# CHAPTER XI

## SPECIAL DEFENSES*

- I. Statute of Frauds — REQUIRES A WRITTEN MEMORANDUM IN CONTRACTS
  1. For sale of real property
  2. For leases of real property
  3. When not to be performed within one year
  4. In consideration of marriage
  5. To answer for debts or defaults of others
  6. For sale of personal property above specified value
- II. Statute of Limitations — REQUIRES SUIT TO BE COMMENCED WITHIN SPECIFIED TIME UNLESS
  a. Injury has been fraudulently concealed
  b. Injured party has been under disability
  c. The claim has been revived
- III. Set-off or Counterclaim
- IV. Accord and Satisfaction

**108. Special Defenses.** Not only may one who is sued for a breach of his contract offer in defense the fact that his breach was caused by a violation of duty on the part of the other, by operation of law, or by such impossibility as the law will recognize, which defenses have been previously considered, but he may offer, in defense, his rights under two notable statutes, known as the Statute of Frauds and the Statute of Limitations and generally adopted in all states, or he may defend by proving a set-off or an *accord and satisfaction*. These defenses are discussed in the order named.

*So called to distinguish them from the regular defenses previously enumerated, which go to the merits of the contract.

## STATUTE OF FRAUDS

**109. Origin.** The Statute of Frauds was a famous English statute, enacted in the year 1677, during the reign of Charles II, and declared to be a statute "to prevent frauds and perjuries." The Fourth and Seventeenth sections of the English statute have been embodied in the statutes of nearly all of our states, with few changes.

**110. Purpose.** The Statute of Frauds provided that certain classes of contract were not enforceable in court unless some note or memorandum in writing, signed by the party to be charged, or by his agent, was presented to the court as evidence of the contract. This note or memorandum was sufficient if it plainly indicated that it referred to the contract between the parties, and showed that the party to be charged with an obligation, had signed or initialed it.

The fact that no such note or memorandum in writing exists is entirely a matter of defense, and if the defendant in a lawsuit does not raise the point, he will be deemed to have waived his rights to object to the enforcement of the contract on this ground. This is because the contract is not void if it fails to comply with the Statute of Frauds, but merely not enforceable if the point be raised. The contract not being void, the parties may carry out their oral obligations as they wish. Furthermore, if one party has performed his part of the contract, the other party, by accepting the benefit of such performance, will lose the right to object on the ground that the contract was not in writing. Thus it is said that "performance by one party takes the contract outside the Statute of Frauds."

**111. Provisions.** The statute as adopted generally throughout the United States provides that the following classes of contracts will not be enforced by the courts unless there be some note or memorandum in writing signed by the party to be charged:

*From the Fourth Section.*

I. Contracts for the sale of any interest in lands;

II. Leases of land for more than one year (with a limited number of exceptions);

III. Contracts by their terms not to be performed within one year;

IV. Contracts made upon the consideration of marriage, except mutual promises of marriage;

V. Contracts to answer for the debt, default, or miscarriage of another;

*From the Seventeenth Section.*

VI. Contracts for the sale of goods, chattels, or things in action for the price of fifty dollars or more, unless:

(*a*) The buyer receives a part of the thing purchased, or

(*b*) The buyer pays part of the purchase price, or

(*c*) The sale be by auction.

**112. The memorandum.** While the statute provides only for a note or memorandum of the agreement, stating its essential terms, careful persons will make a full memorandum, including all the terms, the consideration, the parties, and the conditions to be performed, and will have it signed by both parties. All this is not necessary under the wording of the statute, but if it be done there can be no question as to the sufficiency of the memorandum.

**113. I. Contracts for sale of interests in land** are placed within the statute and its terms apply in every detail to them. Without such a provision, requiring that they be evidenced by writing, fraud could easily be practiced, for with long legal descriptions of land it would be a simple matter for a shrewd, unscrupulous person to mislead another by his verbal statements.

EXAMPLE

A, the owner of land, orally agreed with B to convey it to B upon B's paying the agreed price. B tendered the price, which A refused to accept, saying that he had changed his mind. When B sued A for this violation of the agreement, the court declared that B had no legally enforceable rights against A because no written memorandum of their agreement existed. Shelton vs. Cookay, 138 Mo. App. 389.

**114. II. Leases of land for more than one year** were not enforceable under the English Statute of Frauds unless evidenced by a memorandum in writing. The same provision is adopted in many states of the United States. A few states have modified

this restriction so that it operates only in case of leases for more than three years. In applying these restrictions the courts generally compute the year (or three years) from the date of making the lease, though a few states begin the computation at the time the tenant is entitled to enter into possession of the land. Unless the statute states that the term begins at the time of the date of the lease, the common law rule must be applied, which rule is that the term begins at the date of making the contract.

EXAMPLE

On March first, A orally agreed to rent B's farm for a period of two years beginning April first, and to pay B $500 annually. Nothing was paid, however, and later A refused to accept the premises. When B sued him for violating the contract A said that he did not have to take the farm because of the Statute of Frauds. The court upheld him in his refusal to continue the contract on this ground as the law of the state required contracts for leases of land for more than one year to be in writing. Barlow vs. Wainwright, 22 Vt. 88.

**115. III. Contracts not to be performed within a year** are those contracts which by their terms cannot possibly be performed within that time. These must be in writing, as provided by this statute. If the contract be one for the performance of services for an indefinite time, or is based upon a condition which may happen within a year, or is a contract which one party, though not the other, may perform within a year, no written memorandum is necessary.

EXAMPLE

Drew purchased some lots from Wiswall under an oral agreement that as soon as he built a house Wiswall would construct a street. He built the house but Wiswall refused to construct the street, claiming that the work was not done in one year and that the agreement was unenforceable because not in writing. The court decided that written evidence was not necessary, because the agreement could have been performed within a year, even though it was not so performed. Drew vs. Wiswall, 183 Mass. 554.

**116. IV. Contracts in consideration of marriage** are seldom made in modern business. They were formerly made with the prospective groom by the parent, guardian, or relative of the prospective bride, and by them the former agreed to pay, or settle upon, the bride a certain amount of money at the time of the marriage. Such agreements were not enforceable unless they were in writing.

At present such contracts are rarely made, except in an occasional instance in which a prospective husband promises to settle a certain amount of money on his wife. This is called an *ante-nuptial* agreement and must be evidenced by writing. On the other hand, the mutual exchange of promises to marry need not be evidenced by writing, and such a promise, if broken, will give cause for an action for breach of promise without any written proof.

EXAMPLE

John S. Rowell promised to settle a specified amount of money on his intended bride, provided she would marry him. The agreement was never reduced to writing, and when after their marriage the wife attempted to enforce the contract, the court declared that she could not do so because there was no memorandum in writing. This contract did not come within the exception because the consideration was not the mutual exchange of promises to marry, but the payment of money. Rowell vs. Barber, 142 Wis. 304.

**117. V. Contracts to answer for the debt or default of another.** These contracts are of importance to every business man. Frequently one presses a man who owes him for payment of an account, and satisfies himself with the promise of a third person to pay the debt, if the debtor does not. Yet such an agreement cannot be enforced unless it is in writing, and not even then unless a consideration be given the guarantor. Or it may be that Ames goes to a store with Bates, who wishes to buy goods, and says to the store-keeper, "This is Bates, who wishes to buy some goods. If he does not pay you, I will." The promise of Ames cannot be enforced if it is not in writing. If, however, in the foregoing example, Ames had said, "Let Bates have what he wishes, and charge the goods to my account," his promise would be enforceable, because then the merchant would have sold the goods on Ames' sole credit, and Ames' promise would not have been to answer for the debt of another.

EXAMPLE

The foreman of a railroad construction party arranged with a hotel keeper to supply his men with lodging, promising that he would see that the bills were paid, if the men did not themselves pay. The men failed to pay and when the hotel keeper sued the foreman the court refused to enforce the promise because of the statute of frauds. Obert Brewing Company vs. Wabash Ry. Company, 129 S. W. 991.

**118. VI. Contracts for the sale of goods.** This provision of the Statute of Frauds originally applied to cases in which the

value of goods was more than fifty dollars. Some states do not have this portion of the statute.* In adopting the old statute some states have increased the limit to $200,† while a few have decreased it to $30.‡ The Uniform Sales of Goods act, which we shall discuss later in connection with the sales of personal property, places the limit at $50, and has been adopted in some states.

In connection with this provision of the Statute of Frauds it is to be noticed that there are four means by which a contract for the sale of goods in excess of the statutory amount may be made enforceable, the first being to have a note or memorandum in writing. The other means are (*a*) that the buyer shall have received a part of the thing purchased, or (*b*) that the buyer shall have paid a part of the purchase price, or (*c*) that the sale shall have been by auction. In the last three cases, no note or memorandum need exist, to make the contract enforceable.

1. Millard ordered a quantity of clapboards from Cooke, agreeing to pay $400. Cooke immediately began preparing the boards, dressing them down and putting them in condition for delivery. Millard refused to accept the boards, and when Cooke sued him he defended on the ground that there was no memorandum in writing. The court refused Cooke recovery. Cooke vs. Millard, 65 N. Y. 359.

2. A ordered a bill of goods amounting to several hundred dollars from B, paying five dollars down when the order was given. A later attempted to get out of his contract obligation on the ground that he had signed no memorandum, but the court said that the part payment made writing unnecessary. Weis vs. Hudnut, 115 Ind. 525.

## STATUTE OF LIMITATIONS

**119. Object.** After the lapse of a reasonable period the law will not offer its aid to an injured party. The law will not help a man who has "slept on his rights" too long. Statutes have been adopted in the various states naming a limit of time

* Alabama, Arizona, Delaware, Illinois, Kansas, Kentucky, Louisiana, New Mexico, North Carolina, Ohio, Pennsylvania, Rhode Island, Tennessee, Texas, West Virginia, Virginia.

† California, Idaho, Montana, and Utah.

‡ Maine, New Jersey, Missouri, Arkansas; it is $33 in New Hampshire; $40 in Vermont; and applies to all contracts regardless of value in Florida and Iowa. In the majority of states the limit of value is $50, as under the English statute.

in which law-suits to recover damages must be brought, if at all. These statutes are frequently called statutes of repose, for after the stated time the right of action is at rest so far as the law is concerned. Thereafter only a moral, but not a legal, obligation continues.

**120. Tables of limitation.** In adopting these statutes of limitation, or repose, the various states selected different periods of time for different kinds of actions. The principal classes are actions on open accounts, demands on written contracts, and demands on judgments. There is also a difference in case the contract be under seal, in which event the period of limitation is usually longer than on a simple contract. After the expiration of the time in which the action must be brought, if at all, the claim is said to be "barred by the Statute of Limitations," or "outlawed."

At this point, examine the "Tables of Limitation," in the appendix.

**121. When time begins to run.** Generally the time mentioned in the statute begins to run from the very first day on which an action could properly have been brought, even though the party injured did not know that he had such a right of action until long afterward. In a running account, as for merchandise, and on a note on which some payments have been made, the time begins to run from the date of the last payment or purchase. The payment of interest will have the effect of keeping a debt alive for the full statutory time after payment. An important distinction is also observed in courts of equity, which have declared that fraud of the wrongdoer, preventing the discovery of the right of action, will prevent the time from beginning to run until the fraud is discovered.

EXAMPLES

1. Ames owes Bates $200 on a note due on August 1, 1904. The statute of limitations on notes is six years in their state. In December, 1911, Bates sues Ames on this indebtedness. Ames claims that the note is outlawed, but Bates shows that Ames paid interest up to January, 1909. This prevents the statute of limitations from beginning to run until that time.

2. Call owes Dale for groceries, some having been purchased in 1905, some in 1906 and some in 1907. Dale sues Call for the entire account in 1912, the statute of limitations in his state on such accounts being six years. Call

claims that a part of the account is outlawed, but this is not true because the statute only begins to run from the date of the last item.

**122. Saving clauses.** There are certain provisions, called "saving clauses," which provide excuses in some instances for not bringing the action within the time limit. If the person injured is an infant, an insane person, or a person imprisoned; or if the wrong-doer is absent from the state, the law will excuse failure to bring the action within the time of limitation. These excuses are called "disabilities," and the person who objects to his claim being outlawed on any of these grounds is said to be laboring under a disability.

As a rule, if the disability exists at the time the plaintiff begins to have the right to bring his law-suit, the statute does not begin to run until the disability has been removed. Except in case of one's absence from the state, which inures to the benefit of the other party, all the disabilities extend only to protect the person disabled.

The Statute of Limitations has no effect on actions in which the state sues in its sovereign capacity. Thus a state does not lose its right of action for debt on delinquent taxes, by the lapse of time.

EXAMPLES

1. Perry maintained a cess-pool on his land for a number of years, without protest from the state authorities. It was admitted, however, that the state could have ordered him to remove it at any time on the ground that it was a public nuisance. After many years the state brought an action for this purpose and Perry defended on the ground that the Statute of Limitations barred the action. The court declared that the state could maintain its action. Commonwealth vs. Perry, 139 Mass. 198.

2. A girl six years of age suffered an injury by another person taking possession of her land. Later she became of legal age and commenced an action to recover possession of the land. The wrong-doer defended on the ground that any claim which she might have had was outlawed. The court allowed recovery because the girl had been under disability and the statute of limitations did not affect her rights during that period. Bunce vs. Wolcott, 2 Conn. 27.

**123. Revival of claims.** Even though the lapse of time under the Statute of Limitations may have barred the claim, it is possible for the parties to revive any right which originally existed, by an express promise to do so, and no consideration is needed for this promise. If the debtor, or person who may

claim the benefit of the lapse of time under the statute, makes such an express promise to revive the debt, or makes a payment on the debt, the claim is revived and the Statute of Limitations again begins to run from the date of the new promise. In a few states, the promise to renew the debt must be in writing.

EXAMPLE

Ames owes a debt to Bates, which is allowed to run until it is outlawed by the statute. After this Ames writes to Bates, acknowledging the debt, and stating that he would pay it as soon as he could. This revives the debt and the statute begins running anew.

Payment on a debt after it is outlawed revives the debt.

## SET-OFF AND COUNTERCLAIM

**124. Set-Off and Counterclaim.** When suit is brought against a debtor, he may, in the same suit, defend on the ground that the person who is the plaintiff in the suit is actually indebted to him, the defendant. Litigation is often simplified in this manner, for the validity of the claims of both parties may be then tested in the same suit. The party whose claim is the larger will be awarded the judgment for the amount of the difference in the claims. If the claim of the defendant is a definitely ascertained amount, his defense is called a *set-off*. If the defendant's claim is based on damages which must be ascertained the defense is called a *counterclaim*. In some states the latter is called a right of *recoupment*.

EXAMPLES

1. A owed B the sum of $100 on a contract to repair a building. When B brought a suit to recover this amount, A showed that the contract had not been fulfilled according to its terms and that he had been obliged to pay out $125 to repair the damage which B had caused him. The court allowed A to have judgment against B for $25. McGuire vs. Bransfield, 147 Ill. App. 541.

2. Ames owes Bates fifty dollars for groceries. Bates owes Ames twenty dollars for coal. If Bates sues Ames, Ames may defend by way of set-off and Bates can recover judgment only for thirty dollars.

3. A agreed to work as a salesman for B on a salary and commission, devoting all of his time to B's work. As a matter of fact, A carried a side-line of goods, which he sold for his own benefit, and B discharged him on learning this fact. A sued B for his salary and commissions, but B was allowed to counterclaim and recoup for A's lack of diligence in seeking his own customers, and for the time which he had devoted to this side-line. Alberts vs. Stearns, 50 Mich. 350.

**125. Accord and Satisfaction.** A fourth special defense to a suit for the violation of a contract may be set up, called an *accord and satisfaction*. When there has been a breach of contract on the part of one party the parties may agree on what the one in default is to be required to do or pay by way of settlement. This is a new agreement, and if fulfilled it is a complete discharge of the original contract and no further action can be maintained on the original contract. If, however, it is not carried out, the aggrieved party may sue the other on the original contract, and may recover all the damages which he can prove, even though they be in excess of the amount agreed upon in the accord. The agreement to accept a stated sum, or a specified act, as compensation for breach of a contract is called the accord; the carrying out of the terms is the satisfaction. Both elements must concur to complete the defense.

## PRACTICAL SUGGESTIONS

Don't make oral contracts when written ones are required by law, *because* you thereby furnish the other party with a defense for his refusal to perform.

Don't refuse, however, to perform an oral contract, after the other party has fully performed his part, even though it be a contract required to be written, *because* full performance by one party makes the defense of the Statute of Frauds inapplicable.

Don't postpone collections until they are outlawed, *because* they then cease to be legally collectible.

It is unwise to take advantage of the Statute of Limitations to escape a claim which you should pay, *because* you will thereby destroy your own credit in the community, even though you may have a legal defense.

Try to collect interest or small payments on all bad accounts, *because* such payments prevent the claim being outlawed, and the debtor may some day inherit property and the claim thus become collectible.

It is often wise to sue on debts which are nearly outlawed, *because* you may thereby add many years to their collectibility.

It is futile to sue a man if you owe him as much as he owes you, *because* his right of set-off against you is as valuable as your claim against him.

*Don't make verbal contracts when you could as well make written ones. There is less opportunity for dispute later.*

## REVIEW QUESTIONS

1. Miss Withers sued Ward Richardson for $10,000 damages for his failure to marry her, claiming that he had asked her to be his wife, and that she had accepted, but that he had later married another woman. Richardson

admitted all these things, but defended himself on the following grounds: (1) That the consideration of his promise was the marriage of the parties, and that there was no memorandum of the agreement in writing; (2) that they had not intended to be married until three years later, and (3) that he and Miss Withers were first cousins and that marriages between first cousins were illegal and void in their state. Were any of these defenses valid? Why?

2. Hastings offered Bruce $200 for commission if Bruce would find a purchaser for Hasting's 200-acre farm at a specified price. Bruce within two weeks introduced to Hastings a purchaser who offered to buy the farm at the price, but Hastings unreasonably refused to sell to him on the ground that the proposed purchaser had once been divorced. Bruce then sued for his commissions of $200, and Hastings defended on the ground that the agreement between them was one for the sale of real estate and that there was no written memorandum. Was this a valid defense? Why?

3. Bernier sued Cabot for wages for 15 months at $50 a month. Cabot defended on the ground that Bernier had agreed to work for him for two years and had promised not to leave his employ at any time during that period, but that he had left at the end of 15 months, damaging Cabot to the extent of $300, for which Cabot claimed a right of set-off and counterclaim. Would it make any difference whether this agreement was in writing? Why?

4. Ferris, a negro, in 1872, sued Henderson for wages due him for work during the years of 1866 and 1867, claiming that Henderson had compelled him to work for him during that period as a slave, fraudulently keeping him in ignorance of the fact that slavery had been abolished by a constitutional amendment in December, 1865. Henderson defended on the ground that such actions must be brought within four years. What further would Ferris have to show in order to recover? Why?

5. William Jackson died in 1886 and left his house to his son, Robert Jackson, who was born in 1870, and his farm to another son, George Jackson, who was born in 1885. In 1886 Conrad Johnson went upon the farm and occupied both it and the house continuously as his own until 1914 when Robert Jackson sued him to recover his house and George Jackson sued him to recover his farm. Johnson defended on the ground that by the statute of limitations in his state such actions to recover real estate must have been brought within twenty years after he first wrongfully took possession. Were the claims of either, or both, the Jacksons outlawed? Why?

6. What length of time is allowed in which to bring suit in your state, on open account? on a promissory note? on a debt which the court has declared to be due you?

## CHAPTER XII

## MISCELLANEOUS MATTERS

**126. Two Rules of Evidence.** Rules of evidence are ordinarily of interest to lawyers only. There are, however, two rules as to the manner in which facts may be proved which are of the greatest importance to the man of business, and which, unfortunately, are not generally understood by him. The first of these rules is called the *Parol Evidence Rule*, and the second, the *Rule Regarding Transactions with Persons Now Deceased.*

**127. Parol Evidence Rule.** This is a rule of evidence in force in every court where parties seek to prove their claims against others. It is in substance, that if a contract, or other agreement stating the rights of the parties, has been reduced to writing, the writing only is to be taken as the evidence of what the parties intended, and the contract which they created. Oral evidence is not considered in so far as it changes or modifies the terms of the written instrument. The only points on which oral evidence can be used at all in court in such cases, are points on which the written document is ambiguous and further evidence is necessary to show what the parties meant. The exceptions to this rule are too technical to be considered here, but it is of the greatest importance for the business man to know that when he has put his contract into writing, the writing will be taken by the courts to represent the contract which he entered into, and he cannot tell the court later that he left something out, or intended to put something else in. The student has been advised in the chapters on contracts, to make his contracts in writing because there is less opportunity for dispute later. Not only should he do this, but he should be careful that the written contract is clear, and unambiguous, and that it contains the precise terms of the contract which he intended to create and no others. If he does this, he will find that disputes and troubles growing out of contracts will in a large measure be eliminated.

EXAMPLES

1. Ames, a book-agent, solicits a subscription from Bates, and because Bates is a prominent person in the city, offers to sell him the book for five dollars, the regular price being fifteen dollars. Ames tells Bates, however, that he prefers to have him sign the regular blank order for the fifteen dollars, but will only charge him the lesser price. Bates signs the subscription blank. Later, delivery of the book is made by another agent who demands the entire sum of fifteen dollars, and Bates is without remedy, for the court will not allow him to modify his written contract by oral evidence.

2. Call and Brown enter into a contract whereby Brown is to buy an automobile and pay $1500. Call agrees to keep the automobile in good repair for one year. The parties make a written contract, but neglect to put into the contract Call's agreement as to the repair of the automobile. Later, if Call refuses to repair, Brown is without remedy, because the written contract will be assumed to state all the terms of the agreement, and to have superseded any prior oral agreements between the parties.

**128. Second Rule. Proof of Transactions with Deceased Persons.** A person is not allowed to testify as to agreements made with a person who has died, in suits which are brought or defended by the executor or administrator of such deceased person. This is a rule which perhaps affects business men more than any other rule of evidence. If A owes B a sum of money and dies, leaving considerable property, the court appoints a person known as an executor or administrator of A's estate, to manage the estate and divide it among A's heirs. B may then collect his debt against the executor or administrator, if it was a valid claim at A's death, but in proving his claim he cannot testify as to the conversations which he had with A without witness. The result is that he may be totally unable to prove his claim. The reason for this rule is that if a person could testify to obligations incurred during another's life-time, when they could not be denied because of the other's death, there would be great opportunity for fraud. Business should be conducted with this rule in view. The evidence should always be arranged so as to make the proof of the indebtedness easy. This may be done by insisting upon having debts and contracts reduced to writing. A promissory note is to be preferred to an open book account, for then the debtor's signature to the note may be proved by third persons. Similarly, a written contract is always to be preferred to an oral one, for then it may be presented before the court to prove the nature of the claim.

EXAMPLE

Sargent owed Smith $200 on a promissory note, which, however, was not collectible because it had been due more than six years and was therefore "outlawed." Sargent recognized the debt as valid, however, and meeting Smith one day promised that he would pay him. This promise was sufficient to make the note collectible, but, unfortunately for Smith, Sargent died before paying it. In a suit against Sargent's estate, Smith could not testify as to this promise of Sargent, and in default of such testimony could not collect on the note, because the six years had elapsed. Smith vs. Wells, Administrator, 58 N. H. 201.

**129. Assignment of Contracts.** By *assignment* is meant the transferring of the rights of one person under a contract to another, who was no party to the original contract. The *benefits* or rights which one has acquired by means of a contract may be assigned, except when they consist in the right to personal service from another, and are purely of a personal nature. On the other hand, the *liabilities* or duties which rest on one party by reason of a contract cannot be assigned by him to another so as to release him as the party liable. If such an assignment of liabilities be attempted without the consent of all the parties to the original contract, the first party still remains liable to perform all that he agreed in the contract to perform.

EXAMPLES

1. A agrees to buy from B, who agrees to sell, 500 tons of anthracite coal to be delivered in Albany on October first. A then sells his right to receive the coal, to C, who may demand the delivery by B in Albany according to the terms of the original contract between A and B.

2. The White Automobile Company sold an automobile to Amos, contracting to keep it in repair for one year free of further charge. The White Automobile Company then sold its business to Jones & Brown, partners, and notified Amos that Jones & Brown would carry out the contract and that he should look to them for repairs. This is an attempt to assign a liability, and if Jones & Brown fail to carry out the original agreement, Amos may sue the White Automobile Company for breach of contract.

**130. Result of Assignment.** One important result follows, however, upon the assignment of any contract, and this is the continuation of any set-off or counterclaim, which may have existed against the original party who assigned, against the person to whom he assigned his benefits. It is therefore said that a person taking rights under a contract by an assignment takes those rights subject to the same limitations and defenses which existed against the original party.

EXAMPLE

Jordan contracted to sell to Wheeler 5000 bushels of wheat at an agreed price, which Wheeler paid in promissory notes. Wheeler then assigned his right to receive the wheat to Carter, who demanded its delivery from Jordan. Jordan delivered 4000 bushels, but refused to deliver the balance, claiming a set-off against Wheeler because one of Wheeler's notes given in payment had not been paid. He was justified in this because Carter took Wheeler's right to receive the wheat subject to any defense which might have been urged against him.

Another feature regarding assignments of contract rights is that for his own protection any person who acquires such rights should at once notify the other party to the contract that he is the assignee. Otherwise the latter may continue to perform for the benefit of the original party to whom he was bound by the contract, being protected because he is ignorant of the change in parties.

If A owes B $500 on a contract, B might assign his right to receive the $500 to C, but until A is notified of this assignment he would be under no obligation to pay C. If B were dishonest he might still collect the money, and C's only remedy would be against him and not against A.

In closing the subject of the assignment of contracts, attention is especially drawn to these facts: that the person claiming contract rights by assignment, called the *assignee*, takes no other rights than his *assignor*, from whom he acquired his rights, had, and his acquired rights are subject to the same defenses which might have been urged against his assignor; and further that, for his own protection, he must immediately notify of the assignment the party still held bound by the contract. In only one particular form of contract, called a Negotiable Instrument, are these rules subject to any exceptions.

## PRACTICAL SUGGESTIONS FOR WRITTEN CONTRACTS

The business man may rarely be required to draw his own contracts, but it will often be necessary for him to inspect contracts to discover the rights and duties which are thereby created. For this purpose it is well for him to be familiar with the usual forms in which such agreements are made. Should he ever be required to prepare his own contracts he will find the following points and suggestions of value for a working model.

## Arrangement

The following matters should appear in every contract, and it is best to devote a separate paragraph to each, although the 3d, 4th and 5th items are frequently grouped together.

1. Date and names of the parties,
2. Purpose of the agreement,
3. Consideration,
4. Conditions to be performed by each party,
5. Time and place of performance of conditions,
6. Signatures of parties. (Witnesses and seals, when required.)

This suggested arrangement is illustrated in the contract for the sale of a harvest of wheat shown herewith.

## Contract

Date, Names, and Addresses of Parties

THIS AGREEMENT made this 25th day of February, 1916, between Parke Knapp, of Oregon, Illinois, hereinafter called the seller, and George Jenkins, of St. Louis, Missouri, hereinafter called the buyer:

Purpose of Agreement

WITNESSETH that the seller having agreed to sell, and the buyer to buy, certain wheat;

Consideration

NOW in consideration of ninety cents per bushel, the seller hereby sells and agrees to deliver to the buyer at his warehouse at St. Louis, Mo., all the wheat raised and harvested by him on his two farms in Mayburn township,

Place of Performance

Ogle County, Illinois, during the present year.

Conditions

Said wheat is to be delivered at said warehouse in good, clean, and merchantable condition, on or before the

Time of Performance

15th day of September, 1916.

and Payment

The said buyer agrees to pay for the same immediately upon such delivery.

WITNESS the hands of the parties.

Signatures

Signed..... *Parke Knapp*

..... *George Jenkins*

### Further Comments

Clear and concise language is of the greatest importance in drawing contracts. Useless language should be avoided, but every important term should be included, because the written instrument is presumed to include the entire agreement between the parties.

Always state the consideration clearly, as well as the act which each party has promised to perform.

It is the better practice to place each separate element or condition in a separate paragraph, because there will be less opportunity to overlook them, either in drawing the contract or performing it.

The formal opening and closing of contracts suggested in the preceding illustration is of value, in that it is the usual form and shows plainly that the parties intended to make a contract. If, as in some states, it is necessary for contracts to sell land, to be under seal, the usual closing is as follows:

WITNESS our hands and seals the first day and year above written.

Signed *Parke Knapp* [Seal]
*George Jenkins* [Seal]

When witnesses are required, they sign at the left of the contract in a form similar to this:

*Witnesses*
*Adam Smith.*
*Wilbur Young.*

### PROBLEMS

Write contracts suitable for the following situations:

1. Lillian Mauston is to be employed as a teacher in the Brownsville District School for one year beginning September 1, 1915. George McCarthy is the Director of the School District. Miss Mauston is to devote her entire time to the work and is to be paid $65 a month. Her duties are the usual duties of a teacher in a country school, and she is to be excused only in case of her ill-health. She is to lose $4 a day when absent during the term, or is to furnish her own substitute. The school year terminates June 15, 1916, and she is to have four days' vacation at Thanksgiving, two weeks at Christmas,

and one week at Easter, the precise dates to be determined by the trustees of the district.

2. Albert Black, a farm laborer, is to be employed by Austin Marcum, a farmer, for six months, at $30 a month, to be paid every two months. He is to agree to devote his entire time to the usual work about the farm, and Marcum is to furnish his room and board. Should Black be guilty of misbehavior at any time, Marcum is to have the privilege of discharging him and retaining one month's salary for the damages.

3. Walter Grant, who while an infant, bought groceries of Mallery & Stout, grocers, has become of legal age. He wishes to ratify the debt, which amounts to $225, and Mallery & Stout agree that he may pay it in installments of $25 a month, without interest, if he will agree in writing to pay it, and will not sue him if he pays it according to these terms.

4. Henry Morgan wishes to contract with Smith & Cohen, building contractors, they to agree to build him a house on his property, Lot One, Block Two, Dubuque, Iowa, according to the plans and specifications made for him by Shipley Stark, an architect. The contractors are to furnish all materials, begin work in March of the current year, and complete the house not later than October first. Their bid for construction, which Morgan accepted, was $6280. Their work is to be under the supervision of the architect, and all workmanship and materials are to be of the highest grade. They are to keep the building adequately insured during its construction, and to remove all rubbish. They may receive pay in monthly installments on furnishing architect's certificates stating the value of the work then completed, and are to receive seventy-five per cent of the amount represented by such certificates on demand. They will be paid for additions and variations in the plans only when such variations are agreed upon in writing before being made.

**Suggestions in preparing above contracts.** List every item which you wish to include in the contract. Follow the general scheme suggested for all contracts. Devote a separate paragraph to each material matter. State each term in simple, clear and concise language. Supply names and dates.

## REVIEW QUESTIONS

1. A writes to B that he will take 100 barrels of apples at $4.00 per barrel. (*a*) Must B furnish the apples? (*b*) If B desires to furnish the apples, how soon must he accept?

2. A offers by letter to sell his house to B for $1,000. B replied by letter, "I accept, subject to your first putting the house in thorough repair." Is there a contract or not? Why?

3. A agreed to sell a horse to B, each supposing the price was agreed on. Before delivery it transpired that A thought the price was to be $175,

while B thought it was to be $125. Was there a sale? Why? Suppose this misunderstanding was not disclosed until after delivery, what would be the rights of the parties?

4. In the above case, no delivery having been made, B writes to A that he will split the difference, and adds, "If I do not hear from you by return mail, I shall consider the horse mine." A gets the letter but does not reply. Is there a contract? Give reasons.

5. A contracted to deliver a cargo of lumber on board a vessel within ten days. He began the delivery, but a sudden frost made it impossible to bring any more lumber from the mills by boats navigating the canal. For this reason the work was delayed twenty days. Is A liable, and why?

6. A, in ignorance of the fact that B is an adjudged lunatic under guardianship, enters into a contract with him. Can B's guardian enforce the contract? Would your answer be different if B were a minor instead of a lunatic? Why?

7. A agrees orally to purchase a house and lot of B at a certain stipulated price. They are to meet on a future day and complete the sale. Before the day mentioned, B writes A that he will not make the sale at the price agreed upon. What remedy has A?

8. A, a minor, agrees to sell B a horse for $250. (*a*) Suppose before delivery A refuses to be bound. (*b*) Suppose delivery has been made and money paid when A insists on a rescission. (*c*) Suppose that B sells the horse to C and then A rescinds. What are the rights of the parties in each case?

9. A, in the presence of several persons orally hires B for one year beginning the following September first, at a yearly salary of $1800. B enters upon his employment and continues for seven months, when he is discharged through no fault of his own. Can he recover from A, and if so how much?

10. A owes B a sum of money. C, for a valuable consideration, agrees with A to pay his debt to B. Should this contract be in writing? Why?

11. F sells property to G, intending to put the proceeds beyond reach of creditors. Can G, knowing all the facts, hold the property as against the creditors of F? Can he hold it as against F's creditors, if he had no knowledge of F's scheme? Give reasons for your answers.

12. A dispute arose between A and B as to the amount due from B to A. A claimed $90 while B conceded only $60. Under these circumstances what is the best thing for B to do? If A sues B for $100 what can B do, if anything, to relieve himself from coets and what will be his defense? If upon trial it is found that $60 only is due, who must pay the costs and why?

# CHAPTER XIII

## NEGOTIABLE INSTRUMENTS

- I. Essentials
  - 1. In writing
  - 2. Payable in money
  - 3. Payable absolutely
  - 4. Negotiable in form
  - 5. Payable in specified time
- II. Kinds
  - 1. Checks
  - 2. Drafts
  - 3. Notes
- III. Rights and Liabilities of Parties
  - 1. Maker's or Acceptor's Contract
  - 2. Drawer's or Indorser's Contract
    - a. Conditional liability to pay
    - b. Warranties
  - 3. Rights of Holder in Due Course
    - a. As against
      - 1. Maker, Drawer, or Acceptor
      - 2. Prior Holders
    - b. May depend on
      - 1. Presentment for acceptance
      - 2. Presentment for payment
      - 3. Proceedings on dishonor

**131. Inadequacy of Assignment.** As we have seen, any contract may be assigned if the assignee is willing to accept it subject to the defenses that might have existed against it in the hands of the original holder. Such an assignment, how-

ever, does not facilitate business, because a purchaser of rights under a contract could never be entirely certain of realizing the full value of the thing he thought he was buying, for there might be set-offs against it. Not only might there be set-offs, but if the original contractor had been guilty of fraud which might have been a defense against him, the same defense could be urged against his assignee. These uncertainties would seriously interfere with the free circulation of such contracts among business men.

**132. Negotiability.** Certain forms of business papers, such as checks, notes, and drafts, pass freely from hand to hand, the law protecting the holder in his right to collect face value at maturity from the party originally responsible for its payment.

If Ames gives his note for $100 to Bates, Smith has a right (if the note is properly made out and passes under proper conditions) to assume that the note is worth its face value, $100, and he may buy it for $100 without fear that Ames in paying it will hold back a part in settlement of any debt Bates might owe Ames, or that it might be subject to a defense of fraud. The law covering such cases requires Ames to pay the full amount called for by the note.

Such papers are said to possess the quality of negotiability, or easy negotiation. To be negotiable, a paper must possess certain elements, and must pass from hand to hand under certain conditions. What these elements and conditions are, and what are the principal negotiable instruments, it is the purpose of this chapter to show.

A brief history of negotiable instruments will be of interest at this point.

**Origin.** Under the old rule of the common law, contract rights could not be assigned. Later, assignment was permitted, but this was still unsatisfactory to merchants, owing to the inadequacy of assignment, previously discussed.

Existing laws being unsatisfactory, merchants began to make their own rules, under which checks, notes, and drafts were permitted to pass freely from hand to hand, purged of all claims against them when once they passed into the hands of third parties, under proper conditions.

To enforce these rules, merchants organized their own courts, by which all agreed to be bound. The rules as enforced by these merchants' courts came to be known as the Law Merchant. In the reign of Queen Anne, the rules of the Law Merchant were finally recognized by statute in England, and similar recognition has been given them in other countries.

In the United States the character of negotiable instruments has been recognized by statute in the several states. Minor differences in these state statutes led to much trouble in dealings between merchants in different states. For this reason a conference of lawyers and business men in 1897 formulated the Negotiable Instruments Law (N. I. L.), and efforts have been made to secure uniformity by inducing all the states to adopt this law. The N. I. L. has already been adopted in many states,* and there are prospects of its early adoption by others. States which have not yet adopted the N. I. L. are still governed by their own original statutes, in matters concerning commercial paper.

**133. Assignability Contrasted with Negotiability.** The principal difference between a negotiable instrument and an ordinary contract to pay money lies in the distinction between *assignability* and *negotiability*.

**Assignability** is the quality by virtue of which contracts and other rights may be transferred to a third party, called the assignee, whose rights are thereafter measured by the rights of his assignor. **Negotiability** is the quality of a certain class of written contracts by virtue of which rights thereunder may be transferred to a third party, called the endorsee, whose rights thereunder are thereafter measured by the wording of the instrument itself. A holder may often secure a better title than the original holder had. This is because in the original holder's hands the paper may have been subject to set-offs or the defense of fraud, which could not be urged against a subsequent holder in due course.†

In the case of the assignment of a contract it is always necessary for the assignee, in order to protect his rights, to give notice of the assignment to the original debtor. Otherwise the original debtor might pay a prior party and the assignee would lose his

* Alabama, Arizona, Colorado, Connecticut, District of Columbia, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachussetts, Michigan, Missouri, Montana, Nebraska, New Jersey, Nevada, New Mexico, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, Tennessee, Utah, Virginia, Washington, West Virginia, Wisconsin and Wyoming.

† *A holder in due course*, sometimes called an *innocent bona fide holder for value*, is one who under the rules of the Law Merchant receives a title to negotiable paper free from special defenses which might have been urged against a prior holder. The terms are frequently used and in general describe a transferee (one to whom the negotiable paper has been transferred) who has paid value for the negotiable instrument, and who has received the instrument in the usual course of business before maturity without notice of the existence of any defenses. These points are discussed in detail in a subsequent chapter.

right to demand payment. On the other hand, negotiation may take place without the knowledge or consent of the person who signed the negotiable paper, thereby promising to pay its face to whomever might legally hold it at maturity. With these general characteristics in mind it is important to learn what sort of contracts may be *negotiated* instead of merely *assigned*.

EXAMPLES

1. Ames, through fraud, induced Bates to sign and deliver to him a contract agreeing to pay Ames $50.00 at a given time. Ames sold and assigned this contract to Call for a money consideration, Call knowing nothing about the original transaction. Nevertheless Call was not able to collect on the contract from Bates because of the fraud in the original transaction.

2. Dake, through fraud, secured a negotiable note from Fell, and sold and endorsed it at once and before maturity to Goes for a money consideration. Goes knew nothing of the transaction between Dake and Fell. At maturity he brought suit against Fell to recover the amount of the note and as he was a holder in due course was allowed to recover the amount of the note. If this paper had remained in Dake's hands, Fell could have urged the fraud in defense of a suit to collect it.

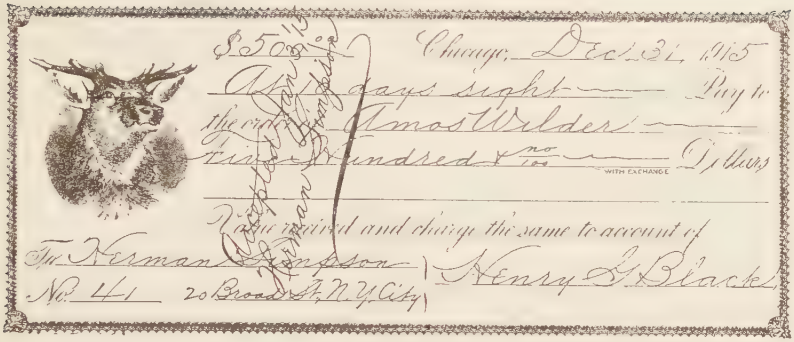
**134. A Negotiable Instrument** is a written contract possessing certain necessary elements, and which when transferred under certain conditions, passes to the purchaser free and clear of any defenses that might have existed against it in the hands of the original holder.

It is a special form of contract to pay money. The four elements of the ordinary contract—competent parties, mutual agreement, consideration and legal subject matter—are necessary to its validity. When it is about to be, or has been, transferred, other requirements are necessary to impart to it the added quality of negotiability. These are, that the instrument must be,

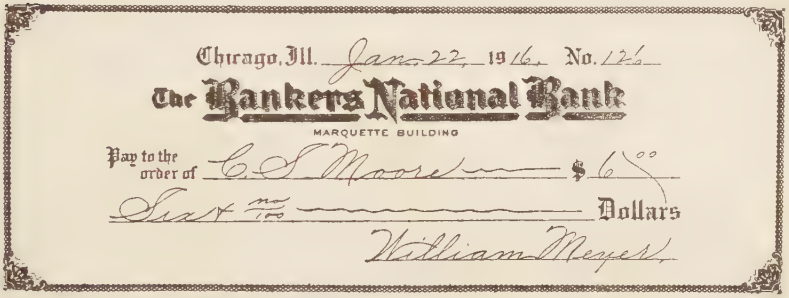
1. In writing,
2. Payable in money,
3. Payable absolutely,
4. Negotiable in form, and
5. Must have definite date of payment.

**135. Forms of Negotiable Instruments.** Negotiable instruments are of three kinds. These are drafts, checks, and notes, each of which is treated in detail in a subsequent chapter. The following are typical forms of each:

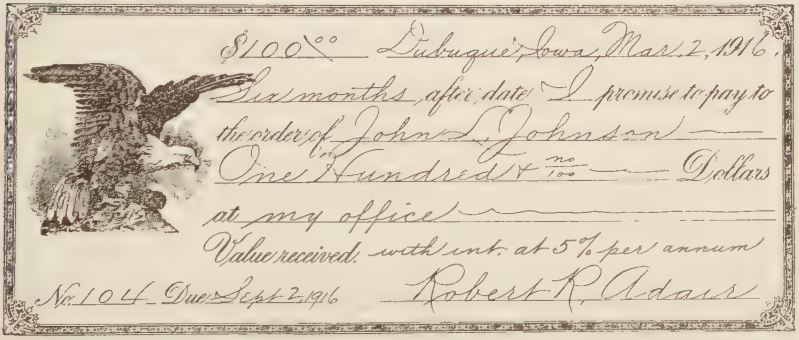
Draft or Bill of Exchange


$500.00
Chicago, Dec. 31, 1915
days sight Pay to
the order of Amos Wilder
Five Hundred & no/100 Dollars
WITH EXCHANGE
Value received and charge the same to account of
To Herman Thompson
No. 41 20 Broad St, N.Y. City
Henry L. Black

Check


Chicago, Ill. Jan. 22, 1916 No. 124
The Bankers National Bank
MARQUETTE BUILDING
Pay to the order of C. S. Moore $ 6.00
Six & no/100 Dollars
William Meyer

Note


$100.00 Dubuque, Iowa, Mar. 2, 1916
Six months after date I promise to pay to
the order of John L. Johnson
One Hundred & no/100 Dollars
at my office
Value received, with int. at 5% per annum
No. 104 Due Sept. 2, 1916 Robert R. Adair

**136. Parties.** It has been seen that competent parties are essential to the validity of all contracts. This includes contracts evidenced by negotiable instruments. The parties to a nego-

tiable instrument may be divided into, (1) original, or those who are named in the instrument, and (2) subsequent, or those into whose hands it may fall later.

The original parties must all be designated with certainty. This is necessary in order that he who is to pay may know to whom or for whom payment should be made, and that he who is to receive payment should know from whom to demand it. The original parties must also be the exact parties named in the instrument, and if the name of one be a forgery, no liability is created on the part of the person whose name is forged, not even to a subsequent holder.

When the name of one of the original parties is signed by an agent, in order to charge the principal and not the agent it is necessary for the agent to sign both his own name and that of the principal in some such manner as this, "John W. Jones, by Adam Smith, his agent." If the agent merely signs his own name, even though he add the word, "agent," he himself, and not his principal, becomes one of the original parties to the instrument.

EXAMPLE

*$100.00* CHICAGO, ILL., *Jan. 21, 1916.*

*One Year* AFTER DATE *I* PROMISE TO PAY

TO THE ORDER OF *William Ames*

*One Hundred and no/100* DOLLARS,

WITH INTEREST AT *6* PER CENT PER ANNUM.

*James Brown, Agent.*

The above is a negotiable instrument, called a promissory note. Because of the manner in which Brown signed, he alone is bound to pay the note, and not some person for whom he may claim he was acting as agent, but whose name does not appear.

**137. Made in Writing.** To be negotiable, a contract must be either in writing or printing, or both. In fact a large proportion of the negotiable paper of business is made on printed blanks, only those portions wherein one may differ from another

being inserted in writing. The writing should be in ink, though a negotiable instrument written with a pencil is valid.

**138. Payable in Money.** A negotiable instrument must be payable in money, and not in goods and chattels. If payable in specific articles it becomes a special contract, and loses its character as a negotiable instrument. It may in all other respects be in correct form, and may be transferred by delivery, yet unless it is payable in money it is not negotiable in the sense of giving a superior title to a subsequent party.

The amount to be paid must be stated with certainty, or the means given by which it can be readily ascertained. It is not negotiable if it be a promise to pay a certain amount, "and all other sums which may be due." If, however, there be added to the amount the words, "with current exchange," the paper is nevertheless negotiable, because the amount can be readily ascertained. The amount is usually expressed in both figures and words. If these differ, the written amount prevails in the absence of other evidence.

By the special statutes of two States,* a note or other instrument payable in specific chattels is negotiable, and in some States it has been enacted that even negotiable words are not necessary. Neither of these special rules, however, has been adopted by the N. I. L., which states the rules of the old Law Merchant.

**139. Payable Absolutely.** There must be no condition or contingency attached to the payment. A negotiable paper, it has been said, "is a courier without luggage." It must contain a definite direction or order, or a certain promise, to pay. A mere acknowledgment of an indebtedness, such as "I. O. U. $100," is not generally sufficient to satisfy this requirement, for while a promise to pay may be implied, yet none is expressed. If any condition be attached to the payment, such as, "provided a certain ship arrives," or "when A shall marry," the negotiability is destroyed, because it may be that neither of these conditions will happen. So also if it be payable out of a certain fund, and limited to that fund alone, the instrument is not negotiable, for the fund may not prove sufficient. A note to be payable "ten months after my death," is absolute in form,

* Indiana and Minnesota.

because the maker is certain to die, and the note will then be payable out of his estate.

If a note is made payable by installments, with a condition that if default be made in the payment of any installment, the whole shall be immediately payable, this form is not so uncertain as to destroy the negotiable character of the instrument of debt.

If the student will remember that the object of negotiable paper is that it may serve as a substitute for money in facilitating the exchange of money, the reasons for these rules will be easily seen. It was the aim of the Law Merchant to give the character of negotiability only to such paper as really corresponded to money as a medium of exchange, and, of course, the only promises that can approximate the quality of money are promises to pay a certain sum absolutely and at all events.

EXAMPLES

*Mission, Outagamie Co., Wis., June 1, 1897.*

*To Buckstaff-Edwards Co.:*

*Please pay to the order of G. E. Woodward and Ed. Erickson, the sum of $600, the same to be the last $600 due me on my contract, and charge the same to my account.*

*Joseph Smith.*

This instrument was in the form of a draft, but the addition of the words, "the same to be the last $600 due me on my contract," limited the payment to whatever sum was actually due on the contract, and as there was no ready means of knowing whether this was more or less than $600, the court decided that the draft was not negotiable. Woodward vs. Smith, 104 Wis. 365.

2. If, however, in the above example the objectionable words had been substituted by the words, "on account of contract between you and me," the payment would not have been limited to the fund due on this contract, but any excess would have been payable absolutely because no direction was given to pay the whole sum out of a particular fund. In such a case the draft would have been negotiable. The courts incline toward holding paper negotiable, and construe such provisions as being merely directory to charge to the specified fund so far as it shall suffice, and to pay the excess out of other funds, where it is possible to do so. First Nat. Bank vs. Lightner, 74 Kans. 736.

**140. Negotiable in Form.** This means that the written instrument must contain negotiable words. The instrument must show on its face that the parties intended that it should pass from hand to hand, and not be limited to remain in the hands of the original holder. The recognized words of negotiability are "bearer," "or bearer," and "or order."

**141. Specified Date of Payment.** Like all written contracts, negotiable instruments should be dated, but this is not absolutely necessary. They should, however, state the time when due, or at least give the facts by which this can be determined readily. This is for two reasons: (1) That the holder may know when to demand payment, and (2) that the time may be fixed when the statute of limitations begins to run, which is always the date on which the note became due. The common expressions in this connection are "on demand," "at sight," "_____days after sight," and "_____days from date," and these are sufficiently definite.

An instrument may be antedated or postdated, provided this is not done for an illegal purpose, and when the date is given in this manner, even though it is not the actual date on which the instrument was made, it is the one used in determining the date when the instrument will become due, called its *date of maturity*. If the date is left blank, any holder has the right to insert the true date on which the instrument was made; and should he insert an improper date, the parties will still be bound by the date so inserted when the instrument has, by indorsement or delivery, passed into the hands of a holder in due course. If the date is left blank by all the parties the time will be computed from the date on which the instrument was actually made.

**142. Delivery.** In addition to the above essentials of the paper itself, it must be delivered before it has effect. If an otherwise valid instrument gets into circulation without the consent and through no fault of the maker, the maker will not be liable on it.

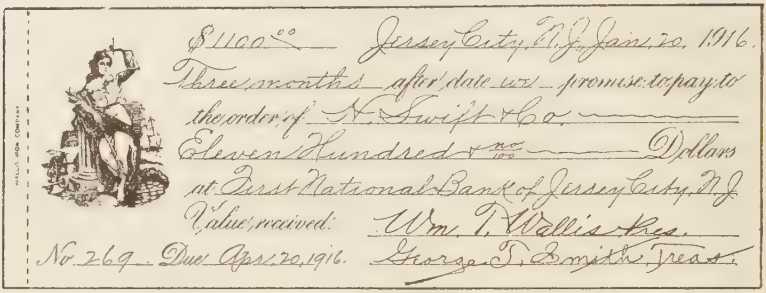
EXAMPLE

Ames writes out a note payable to bearer which he intends to deliver to Bates. Call, who is standing near by, seizes the note as Ames writes his name on it, and runs out, transferring it to Smith, an innocent *bona fide* holder. Smith cannot enforce the note against Ames, because Ames never delivered it.

The qualities so far discussed are essential to the validity of all forms of negotiable paper. In the next three chapters the three forms of negotiable instruments commonly used in business, are described and discussed. These, as previously stated, are drafts, checks, and notes.

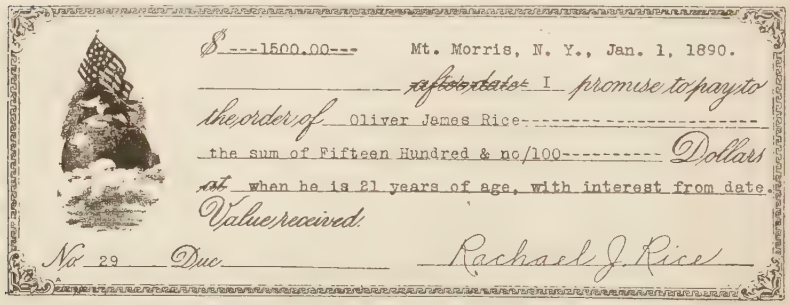
## REVIEW QUESTIONS

1. Inspect the following promissory note:


$1100.00 Jersey City, N. J. January 20, 1916.
Three months after date we promise to pay to
the order of H. Swift & Co.
Eleven Hundred & no/100 Dollars
at First National Bank of Jersey City, N. J.
Value received. Wm. P. Wallis Pres.
No. 269 Due Apr. 20, 1916. George T. Smith Treas.

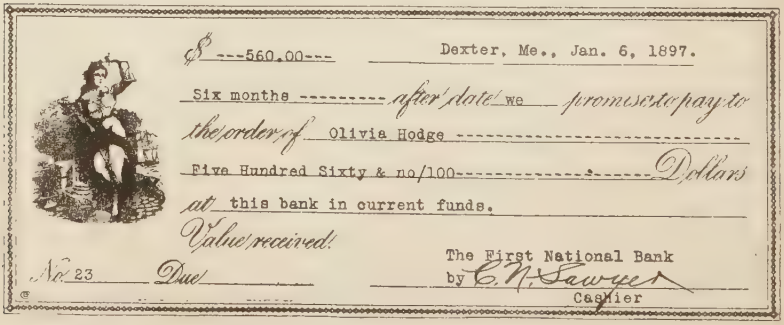
When this note was not paid H. Swift and Company brought suit against the Wallis Iron Company. Could they recover the $1100 from the Wallis Iron Company? Could they have recovered this amount from Wallis and Smith personally? Why?

2. Inspect the following promissory note:


$ ---1500.00--- Mt. Morris, N. Y., Jan. 1, 1890.
~~after date~~ I promise to pay to
the order of Oliver James Rice
the sum of Fifteen Hundred & no/100 Dollars
~~at~~ when he is 21 years of age, with interest from date.
Value received.
No 29 Due Rachael J. Rice

Is this a negotiable instrument? Why?

3. Inspect the following promissory note:


$ ---560.00--- Dexter, Me., Jan. 6, 1897.
Six months after date we promise to pay to
the order of Olivia Hodge
Five Hundred Sixty & no/100 Dollars
at this bank in current funds.
Value received.
No 23 Due
The First National Bank
by C. N. Sawyer
Cashier

Is this a negotiable instrument? Why?

4. Inspect the following instrument:

RUTLAND AND BURLINGTON RAILROAD COMPANY

*No. 253* *$1000.00*

BOSTON, MASS., *Apr. 1, 1850.*

*In four years from date, for value received, the Rutland and Burlington Railroad Company promises to pay in Boston, to Messrs. W. S. & D. W. Shuler, or order, $1000, with interest thereon, or at its option to transfer to the said W. S. & D. W. Shuler ten shares of capital stock in this company of the par value of $100 each.*

RUTLAND AND BURLINGTON RAILROAD COMPANY,
BY *T. Follett*, President,
*Sam. Henshaw*, Treasurer.

Is this a negotiable instrument? Why?

5. Mary Brown contracts to work for Mrs. Smith as a domestic for $5.00 a week. Mrs. Smith sells her right to Mary's services to Mrs. Jones for $20.00. Can Mrs. Jones compel Mary to work for her at the salary agreed upon by Mrs. Smith? Why?

6. Ames and Bates were partners in a hardware business. Ames bought Bates' interest in the business for $5000, Bates agreeing never again to engage in the hardware business. Within a month after the dissolution Bates had again started in the hardware business in the same city. What could Ames do about it? Why?

7. On June 15, 1915, Ames loaned Bates $200.00 in cash in the presence of Call. A month later, Bates and Call were both killed in a train wreck, Ames sued the estate of Bates for $200. Was he allowed to recover? Why?

## CHAPTER XIV

### DRAFTS

- I. Parties
  - 1. Original
    - a. Drawer
    - b. Drawee—Acceptor
    - c. Payee
  - 2. Subsequent
    - a. Indorser
    - b. Transferrer without Indorsement
- II. Forms
  - 1. Payable on Demand
  - 2. Payable at Sight
  - 3. Payable after Sight, or Time Instruments
- III. Acceptance
  - 1. Express
  - 2. Implied
  - 3. Virtual
  - 4. For Honor
  - 5. Qualified

**143. Introduction.** The most common kinds of negotiable instruments are the draft, or bill of exchange, the note, and the check. The oldest of these is the draft, and it was the first one to be recognized by the law courts as negotiable.

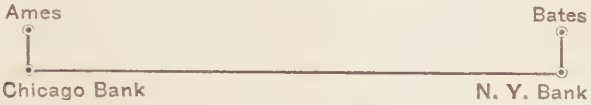
Drafts were originally called bills of exchange, a name derived from the French *billet de change*, and were first used to avoid the dangers in sending actual money a long distance.

EXAMPLES

1. Suppose A, in Havana, Cuba, owes B, in Chicago, five thousand dollars. C, who is about to go to Havana from Chicago, pays B five thousand dollars, and receives from B a draft which entitles him, on reaching Havana, to receive five thousand dollars from A. All the parties are accommodated by this arrangement, for A does not have to risk his money by sending it to

Chicago, B gets his money without danger of loss, and C travels to Havana without the risk of being robbed *en route*.

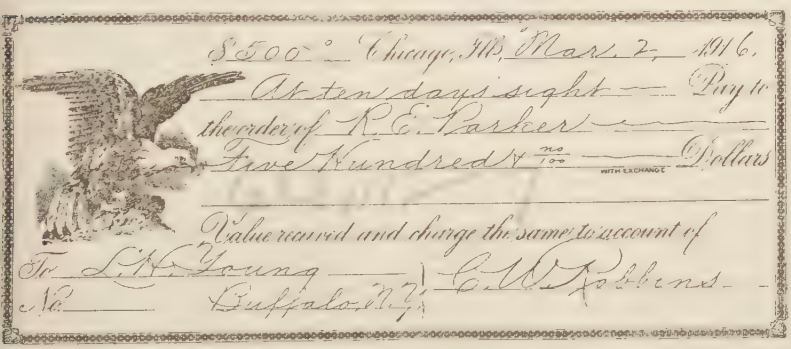
2. Ames, of Chicago, owes Bates, of New York. Bates draws on Ames, naming a New York bank as payee. The New York bank sends the draft to a Chicago bank, which collects from Ames and credits the New York bank, which then pays Bates.




**144. A Draft** is an unconditional order in writing, signed by the person giving it, directing a second person to pay to a third person, or order, or bearer, a certain sum of money on demand, or at a fixed future time. A draft drawn on a person in another country, or another state in the Union, is called a foreign bill of exchange, while if it is drawn on a person in the same state, it is called an inland bill of exchange.

**145. Parties to a Draft.** There are three original parties to a draft, and there may be any number of subsequent parties. The person who signs the draft is the *drawer*; the one to whom it is addressed and who is asked to pay it, is the *drawee*; and the one to whom it is payable is the *payee*. If the draft is accepted by the drawee (*i.e.*, he agrees to pay it), he is then called the *acceptor*. The subsequent parties to a draft are those to whom it is passed either by indorsement and delivery or by delivery without endorsement, after the first delivery.

EXAMPLE


$500 Chicago, Ill. Mar. 2, 1916.
Ten days sight Pay to
the order of R. E. Parker
Five Hundred & no/100 Dollars
WITH EXCHANGE
Value received and charge the same to account of
To L. H. Young C. W. Robbins
No. Buffalo, N. Y.

In the above form, Robbins is the drawer, Young the drawee, and Parker the payee. The substance of it is that Robbins

requests Parker to demand $500 from Young, and at the same time requests Young to pay this amount to Parker.

**146. Acceptance of a Draft.** Young is under no obligation to pay Parker according to the demands of the draft, until he "accepts" it, that is, until the draft is presented to him and he expresses his willingness to pay it. It will be noticed that the draft itself contains no promise from Young that he will pay it; in fact, until it is presented to him, he may not even know of its existence, although it is customary for the drawer to notify the drawee that he will draw upon him, unless there is an understanding that such notice is unnecessary.

**147. Form of Acceptance.** In form, an acceptance usually consists of the word "accepted" written across the draft by the drawee, together with the date of acceptance and the signature of the drawee. In the above example Young would accept the draft writing across its face the words, "Accepted, March 5, 1916, L. H. Young." He is then obligated to pay $500 to Parker, or to any person to whom Parker may transfer the instrument, in ten days from the date of acceptance. (In states allowing days of grace, he would be given three additional days.) Instead of the word "accepted," the word "seen," or "honored," is frequently used by acceptors and is equally effective, or a draft is accepted if the drawee merely writes his own name across the face.

Acceptance of a draft must be in writing by the drawee on the draft itself, except in three special instances. These are: (1) Implied acceptance, (2) Virtual acceptance, (3) Acceptance for honor.

**148. An implied acceptance** is one in which the drawee, to whom a draft has been delivered for acceptance, by his acts or conduct permits the payee to infer that he has accepted the draft. If Parker presented the draft in the above example to Young and Young retained it, saying that he would attend to it he would be deemed to have accepted it.

The N. I. L., Sec. 137, says in regard to this:

"Where a drawee to whom a bill is delivered for acceptance destroys the same, or refuses within twenty-four hours after such delivery (for acceptance), or within such other period as the holder may allow, to return the bill accepted or non-accepted to the holder, he will be deemed to have accepted the same."

**149. A virtual acceptance** is a promise in writing to accept a draft, but which written promise is made, not on the draft itself, but on a separate paper. Such an acceptance is usually made before the draft is drawn. Suppose, in the above example, Young had written to Robbins prior to March 2, saying that if Robbins would draw on him he would accept the draft. Young would be taken to have accepted the draft in favor of any person to whom his promise to accept had been shown and who had relied on it. Section 134, N. I. L., states the limits of such an acceptance, as follows:

"Where an acceptance is written on a paper other than the bill itself, it does not bind the acceptor except in favor of a person to whom it is shown and who, on the faith thereof, receives the bill for value."*

**150. An acceptance for honor** is an acceptance made by some person other than the drawee. After a draft has been dishonored by the drawee and protested,† a third party may be induced to intervene and accept the paper for the honor of the drawee or any person liable on the draft. This must be with the consent of the holder.

**151. Effect of Acceptance.** When a draft is accepted, a direct contract arises between the acceptor and the holder, and the drawer is then liable to pay only if after proper presentment for payment the acceptor does not pay, and proper notice of this failure to pay is given. The drawer is said to be secondarily liable. If payment is refused by the acceptor, the holder may sue the acceptor or he may protest the paper and sue the drawer or any indorser.

Acceptance is made only upon presentation of the instrument to the drawee, and the drawee may require that such presentment for acceptance shall be made according to business usage.

**152. Qualified Acceptance.** The acceptance may be either (1) general, or (2) qualified. A general acceptance is one by which the drawee accepts and promises to pay the instrument in the exact form and according to the precise demand of the

* The Illinois statute omits the words, "to whom it is shown and."

† "Protested" refers to the action taken by a notary public after a draft has been dishonored. He certifies that he presented the draft and that it was dishonored, and mails notices to all parties named in the draft. This is required in order to hold such parties liable, and will be discussed in a later chapter.

instrument which is presented to him. A qualified acceptance is one by which the drawee promises to pay the instrument according to some new terms, or conditions, not contained in the draft as made by the drawer. A qualified acceptance may be treated as a dishonor by the holder and he may proceed at once against the maker, protesting the draft for dishonor. Or he may take the draft with the qualified acceptance, in which event he releases the drawer and all prior parties unless they specifically give their assent.

EXAMPLES

*No. 246. $500.00* *Chicago, June 22, 1916.*

*At ten days' sight pay to Joseph Wilson the sum of Five Hundred Dollars at the First National Bank, Chicago.*

*(Signed)* *Harvey W. Hulburd.*

To *William Young,*
*Albany, N. Y.*

Young may make a *general acceptance*, if he writes across the face of the instrument, "Accepted, William Young, June 25, 1916," or "Seen, June 25, 1916, William Young," or "William Young." The particular form is immaterial.

The following is also a general acceptance: "Accepted, June 25, 1916, payable at Merchants' Saving Bank, Albany, N. Y., William Young," because the place of payment specified in the acceptance is not declared to be the exclusive or only place of payment.

Young may also make a *qualified* acceptance, if he writes across the face of the draft any of the following phrases:

"Accepted, June 25, 1916, payable at Merchants' Savings Bank, Albany, N. Y., *only*, William Young."

"Accepted, June 25, 1916, for Two Hundred Dollars, William Young."

"Accepted if Wilson sends me the money necessary to pay this, June 25, 1916, William Young."

"Accepted June 25, 1916, to be paid in thirty days, William Young."

**153. The Acceptor Admits** by his act of acceptance the signature of the drawer, and cannot later escape from his promise to pay on the ground that the signature was a forgery. He also admits that he has funds belonging to the drawer, or is himself willing to advance the money necessary to pay the draft when it becomes due, and that the drawer was a person competent to make a legal contract.

The acceptor does not admit that the body of the instrument has not been altered since it left the drawer's hands.

**154. Transfer of a Draft.** The payee of a draft is always its first holder. The meaning of the language used in negotiable paper, whether it be a promise or a direction, is to pay to the person named in the paper, *or* to any one whom he may designate. A draft is therefore transferable by indorsement.

### Demand Draft

$ --300.00-- Chicago, Jan. 27, 1915

On Demand Pay to

the order of Matthew M. Murphy

Three Hundred & no/100 Dollars

Value received and charge the same to account of

To Walter H. Underwood,
4 Anne St.,
No. 42 New Orleans, La.

Simeon E. Baldwin

Baldwin is the drawer, Murphy the payee, and Underwood the drawee. This is a foreign bill of exchange, because drawn by a resident of one state upon a resident of another. Murphy may endorse this to another party, who, upon its dishonor by Underwood would bring it back to Murphy as indorser. No presentment for acceptance is necessary, because it is payable upon presentment.

### Sight Draft

$ ---400.00--- St. Louis, Mo., Jan. 27, 1915

At Sight Pay to

the order of Matthew M. Murphy

Four Hundred & no/100 Dollars

Value received and charge the same to account of

To Walter H. Underwood
4 Anne St.,
No. 43 New Orleans, La.

Simeon E. Baldwin

The parties are the same as in the preceding example. In states which have adopted the N. I. L. the qualities are the same as in a draft payable on

demand. In some other states, days of grace* are allowed on sight drafts, although denied on drafts payable on demand, and presentment for acceptance is necessary before the drawee can be charged with the obligation of paying.

## Time Draft

$ --500.00-- St. Louis, Mo., Jan. 27, 1915.

Thirty days after sight ---------- Pay to

the order of Matthew M. Murphy ----------

Five Hundred & no/100 ---------- Dollars

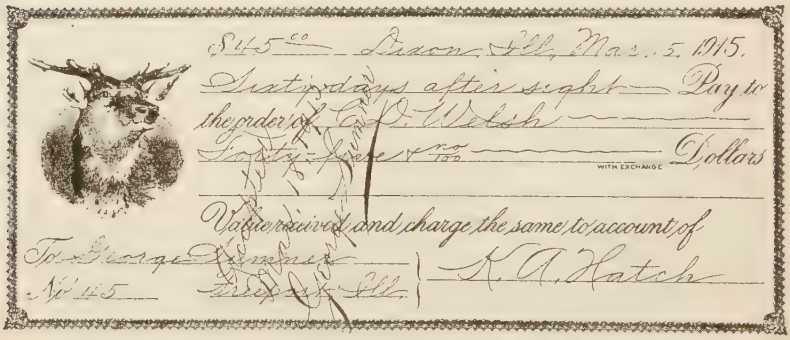
Value received and charge the same to account of

To Walter H. Underwood
4 Anne Street
No. 44 New Orleans, La.

Simeon E. Baldwin

The parties are the same as in the preceding examples. Presentment to Underwood for acceptance is necessary in order to fix the time when the thirty days begins to run, and also in order to charge the parties with their obligations; that is, to charge Underwood with paying $500 to Murphy, or a subsequent holder, and to charge Baldwin with paying if Underwood does not.

## Acceptance


$45.00 Luxora, Ill., Mar. 5, 1915.
Sixty days after sight Pay to
the order of E. D. Welsh
Forty-five & no/100 Dollars
WITH EXCHANGE
Value received and charge the same to account of
To George Sumner
No. 45
Accepted Mar. 18 Ill.
L. A. Hatch

This is an inland bill of exchange. Hatch is the drawer, Welsh the payee, and Sumner the drawee. When Welsh presents the draft to Sumner, Sumner accepts it by writing across the face, "Accepted, March 18, 1915,

* **Days of grace** are three extra days added to the date on which an instrument is due and payable, during which time it could not be sued upon or treated as over-due. They have been abolished in the majority of states. Arkansas, Mississippi, and Wyoming still allow days of grace on all drafts and notes: and Maine Massachusetts, Michigan, Minnesota, Rhode Island, South Carolina, and Texas, on sight drafts alone.

George Sumner." After this is done, Sumner is bound to pay the $45 sixty days after March 18, to Welsh, or to any person to whom Welsh has endorsed the paper.

If Sumner had dishonored the bill and it had been protested by a notary public, Ward, a third party, might have accepted it, with the consent of Welsh. He would then have bound himself to pay it if Sumner should again refuse.

## REVIEW QUESTIONS

1. Inspect the following draft:

*Castine, Me., Jan. 5, 1860.*

*For value received, please pay to the order of G. F. and C. W. Tilden forty dollars, and charge the same against whatever amount may be due me for my share of fish caught on board schooner "Morning Star," for fishing season of 1860.*

*Yours, etc.,*

*Frank R. Blake.*

*To Messrs. Adams & Co.*

*Accepted to pay.—Adams & Co., Jan. 6, 1860*

Is this a negotiable instrument? Why? Who is the maker? payee? drawee?

2. Archer in Boston purchases furniture of Wilson in Grand Rapids, Michigan, of the value of $200. Wilson ships the furniture, and then draws on Archer for the price. How does he do this? Write a draft, designating a Boston Bank as the *Continental Exchange Bank.* The bank in Grand Rapids is *The First National Bank.* How does Wilson secure his money?

3. Inspect the following draft:

$ 45.00 La Crosse, Wis., June 22, 1915, No. 44

Pay to the order of The Union State Bank

Forty Five and 00/100 DOLLARS

Value received and charge to the account of

To M. M. Clarke,
Superior Wis. Mary Wheelan

When this draft is presented to Clarke, he writes across the face, "Accepted, June 22, to be paid half in money and half in bills, M. M. Clarke." Is this a proper acceptance? Why? What is its effect?

4. How is a bill of exchange dishonored? What is the result?

# CHAPTER XV

## CHECKS

- I. Parties
  - 1. Original
    - a. Drawer
    - b. Drawee
    - c. Payee
  - 2. Subsequent
    - a. Indorsers
    - b. Transferrers without Indorsement
    - c. Indorsees and Transferees
- II. Form
  - 1. Ordinary
  - 2. Special
    - a. Certified Checks
    - b. Cashier's Checks
    - c. Bank Drafts, or Checks
    - d. Certificates of Deposit

**155. A Check** is an order drawn against a deposit of funds in a bank, for the absolute payment on demand of a definite sum of money to a certain person, or his order, or to the bearer. A check is similar to a draft, except that it always presupposes the existence of funds on deposit, without which it is worthless.

All that has been said in reference to the use and transfer of a draft applies with equal force to a check, except that acceptance has no function in connection with checks, because they are payable on demand, and presentment for acceptance is not required. Nor is a check ever entitled to days of grace.

There are three original parties to a check. These are the *drawer*, or the one who signs it; the *drawee*, which is always a bank; and the *payee*, who is entitled to receive the money. The contract represented by the check is between the bank and the drawer, consequently if for some reason the bank refuses to pay the check, the holder cannot maintain an action against the bank * and his remedy is against the drawer alone. For the same

* In a few states a check is regarded as an assignment of the deposit, and where this is the case the holder is given a right to sue the bank if the payment of a check is refused on demand. This is the law in Illinois, Kansas, Kentucky, Nebraska, South Carolina, Texas, and Wisconsin.

reason the payee cannot stop payment on a check by notifying the bank, although the drawer can do so.

**156. Relation to Banking.** Checks are of great commercial importance. Business men do not as a rule have proper facilities for protecting their ready money from either fire or robbers. The bank offers them this protection without charge, its compensation being the use which it can make of the money so deposited with it, which it can expect will be left for some time.

In some instances banks fail, and the depositors lose their money. The only cases in which the holder of a check may lose his money because of such a failure are those in which he has long delayed in presenting his check for payment. It is his duty to go to the bank with reasonable promptness (see Sec. 212 of this text) and secure the money which the drawer has, by means of the check, requested the bank to pay. If he delays beyond a reasonable length of time, and the bank fails, he cannot recover the money from the drawer, but must himself bear the loss. This rule is stated in Section 186, N. I. L., as follows:

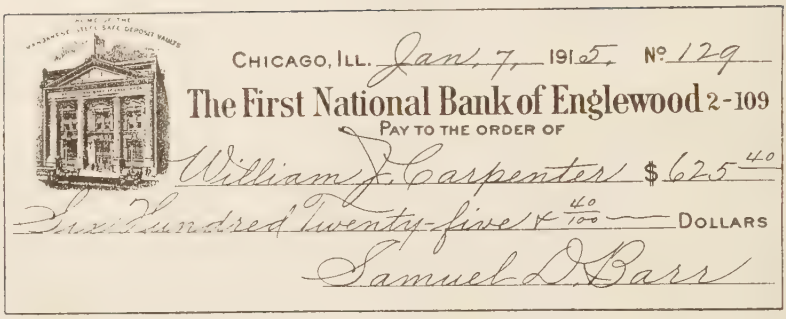
"A check must be presented for payment within a reasonable time after its issue or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay."

**157. Form of Check.** To be negotiable, a check must conform to the general requirements for negotiability. For instance, it must contain the negotiable words "or order," or "or bearer."* It is not safe to make a check payable to cash or to currency or to bearer unless they are to be cashed at once, for if lost or stolen it could be cashed by the finder or thief and the rightful payee would have no redress nor could the drawer claim that the bank had been careless in making payment. The safe method is to make checks payable to the order of a designated person, for in that case the bank has no right to pay any one except that person, or his order.

**158. Special Forms** of negotiable instruments, which are in their essentials checks, are (1) certified checks, (2) cashier's checks, (3) bank drafts, and (4) certificates of deposit.

* Checks payable "to cash" and "to currency" are considered payable to bearer. Checks payable to "Self" must be indorsed before they are negotiable.

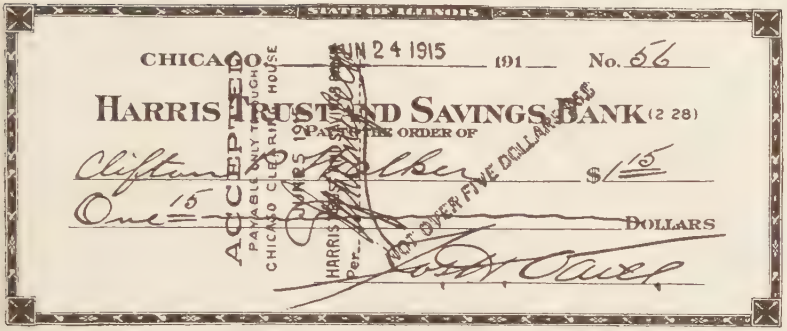
Check


CHICAGO, ILL. Jan. 7, 1915 No. 129
The First National Bank of Englewood 2-109
PAY TO THE ORDER OF
William J. Carpenter $625 40/100
Six Hundred Twenty-five 40/100 DOLLARS
Samuel D. Barr

A check is a form of draft. Note the similarity.

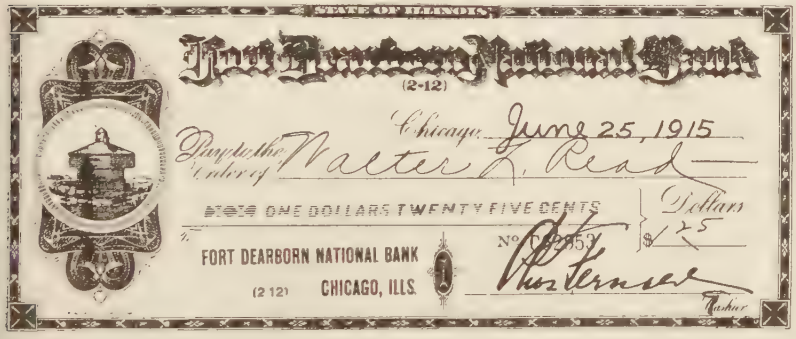
**159. Certified Checks.** If the payee who is about to receive a check, perhaps as payment for goods, is doubtful whether the drawer has to his credit in the bank the amount of money represented by the check, or is fearful that although the drawer may have the money in the bank at the time of giving the check it may be withdrawn before his check is paid, he may insist on a certified check, or he may accept the check and himself take it to the bank for certification at once. A certified check is an ordinary check, across the face of which is written a certification by the bank. The bank makes this certificate by writing or stamping across the face of the check the word, "Certified," or some word of similar import, together with the date and the signature of a proper official of the bank. By this certification the bank agrees to pay the check. It then reserves the amount of the check out of the drawer's deposit. Until this is done there is only the original contract between the drawer and the bank; after it is done a new contract is created between the bank and the payee. After certification a bank is obliged to pay the certified check, even though it should prove to be a forgery, for the rule is that a bank is obliged at its peril to know the signatures of its depositors, and if it negligently certifies a forged check, or if it pays a forged check, it must assume the risk. Certification does not, of course, furnish protection against a subsequent alteration of the check; it is a guarantee to pay the check as it read at the time of certification.

Certified Check


STATE OF ILLINOIS
CHICAGO JUN 24 1915 191 No. 56
HARRIS TRUST AND SAVINGS BANK (2 28)
PAY TO THE ORDER OF
Clifton Holbert $115
One 15 DOLLARS
NOT OVER FIVE DOLLARS
ACCEPTED
PAYABLE ONLY THROUGH CHICAGO CLEARING HOUSE
HARRIS TRUST AND SAVINGS BANK
Per

**160. Cashier's Checks** are sometimes issued by banks instead of certificates of deposit or drafts. A cashier's check is in form simply an ordinary check, drawn on the bank by the cashier in his official capacity, and made payable to the depositor or someone he may designate. It is payable on demand, and has the advantage that the payee may usually receive payment from banks in other cities, if he can identify himself as the payee named, without waiting for it to be returned to the drawee bank. The cashier's check will, however, ultimately have to be returned by any bank so advancing money on it, to the issuing bank, for payment.

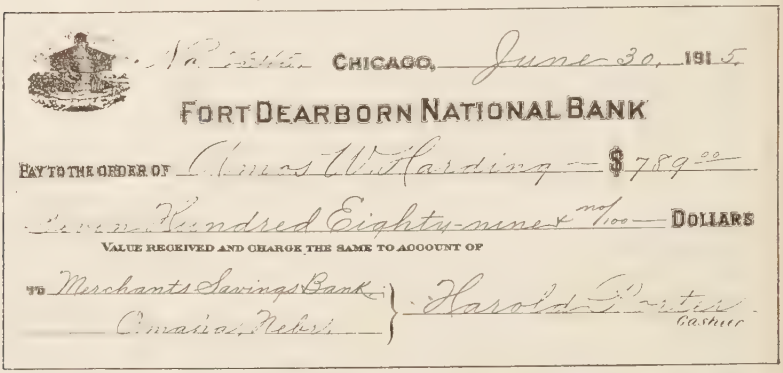
Cashier's Check




**161. A Bank Draft** differs from the ordinary cashier's check in that instead of the drawee being the bank issuing the check, the drawee is a bank in some other city, usually Chicago, New York, St. Louis, San Francisco, Milwaukee, or other central banking point. This has a superiority over the ordinary cashier's

check in that it does not have to be returned to the issuing bank for payment, but is payable at the city of the drawee bank.

**Bank Draft or Check**


No. 2551 CHICAGO, June 30, 1915.

FORT DEARBORN NATIONAL BANK

PAY TO THE ORDER OF Chas. W. Harding — $789.00

Seven Hundred Eighty-nine and no/100 — DOLLARS

VALUE RECEIVED AND CHARGE THE SAME TO ACCOUNT OF

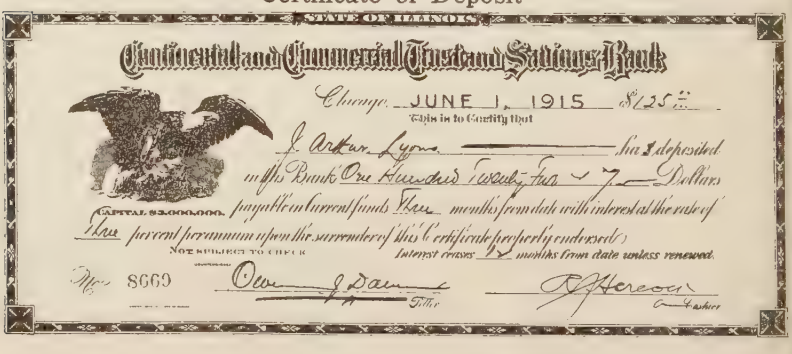
TO Merchants Savings Bank, Omaha, Nebr.

Harold F. Potter, Cashier

**162. A certificate of deposit** is another form of voucher for money deposited in a bank. Instead of desiring to open a checking account, the depositor may merely wish to leave the money at the bank for safe-keeping indefinitely or for a specified period of time on the promise of the bank to pay him interest. If this is done the depositor receives a certificate of deposit which states the conditions of the deposit.

Money deposited, and represented by a certificate of deposit, cannot be drawn out by check. If a portion of it is desired, the certificate may be presented at the bank, and the payment written on the back of the certificate, or the old certificate may be surrendered and a new one issued for the amount remaining undrawn. The latter method is considered to be the better.

**Certificate of Deposit**


STATE OF ILLINOIS

Continental and Commercial Trust and Savings Bank

Chicago, JUNE 1, 1915 $125.00

This is to Certify that

J. Arthur Lyons has deposited

in this Bank One Hundred Twenty-five — Dollars

payable on current funds three months from date with interest at the rate of

three per cent per annum upon the surrender of this Certificate properly endorsed.

NOT SUBJECT TO CHECK Interest ceases 3 months from date unless renewed.

No. 8669 Owen J. Daum, Teller — H. F. Hereon, Cashier

**163. Post-dating.** If a check is dated ahead, it is of no effect until the day of its date. There is always a possibility that there may not be a balance to the credit of the drawer sufficient to cover the check when due, and persons receiving post-dated checks should bear this in mind.

Persons issuing post-dated checks should bear in mind the possibility of the humiliation and injury to credit which would result if the check were dishonored by the bank.

If a check bearing the current date is given in payment of an existing debt, and there are no funds on deposit to cover it, the person issuing it may suffer only the humiliation of having it returned to the one who held it, marked "Not sufficient funds" by the bank. But if it be given as consideration for a new contract, the drawer may find himself liable for obtaining goods or money under false pretenses.

**164. Canceled checks** operate as receipts. If a check be given in discharge of a debt, the payee can secure his money from the bank only by indorsing his own name upon the back of the check, and this indorsement is evidence that the payee got his money.

When the bank submits a statement to a depositor at the end of a month, or other convenient interval, all checks which have been paid are returned to him, and in this way he has proof that he paid to the payee the amount of the check. On account of this feature of checks, they are much used in the payment of debts by business men.

## REVIEW QUESTIONS

1. Jordan places $500 in the People's Bank as a checking deposit. He then draws a check payable to Mills, or order, for $200. Mills presents the check promptly at the bank for payment, but is refused. What rights, if any, has Mills (1) against the bank? (2) against Jordan? Has Jordan any rights against the bank? Why?

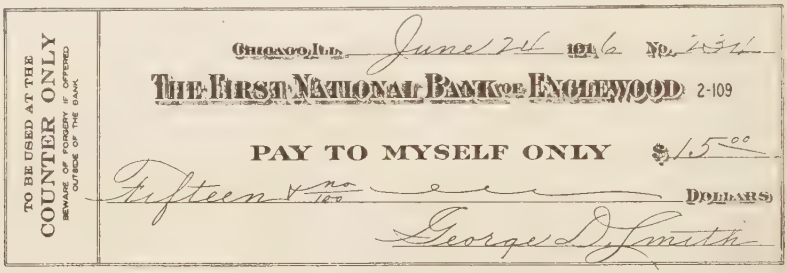
2. Morgan, with a checking deposit of $800 in the Mercantile Bank, issues a check for $400 payable to Barnes. Barnes neglects to present the check for payment, and two months later while the check is still in his possession the bank fails, paying its depositors fifty cents on the dollar. What rights has Barnes (1) against the bank? (2) against Morgan?

3. J. A. Simpson issues a check on the Merchants' Bank for $700 payable to the order of Finney. Finney presents the check at the bank for certification, and Sullivan, the assistant cashier, mistaking the signature for that of J. D.

Simpson, certifies it. As a matter of fact J. D. Simpson has a large checking account, while J. A. Simpson has an account of less than $30. Finney indorses the check to Thompson, who five days later presents it at the bank for payment, which is refused. Who must bear the loss? What rights has Thompson? Finney? The Merchants' Bank?

4. Stevens draws a check on the Farmers' Bank payable to Jones for $100.00, which is certified by the farmers' Bank and delivered to Jones. Jones loses the check and it ultimately turns up in the hands of Brown, an innocent holder for value. By this time the check has been altered in amount to $1000.00 and Jones' signature has been forged on the back. What amount, if any, can Brown require the bank to pay him?

5. What rights, if any, has Jones in the above example?


TO BE USED AT THE
COUNTER ONLY
BEWARE OF FORGERY IF OFFERED OUTSIDE OF THE BANK
CHICAGO, ILL. June 24 1916 No. 1234
THE FIRST NATIONAL BANK OF ENGLEWOOD 2-109
PAY TO MYSELF ONLY $15.00
Fifteen & no/100 DOLLARS
George D. Smith

6. A forger disguised himself as Geo. D. Smith, walked into the First National Bank of Englewood and filled out the counter-check shown above. His disguise was perfect and his imitation of Smith's signature was perfect. The cashier did not hesitate to hand him the money. Who suffered the loss? Why?

# CHAPTER XVI

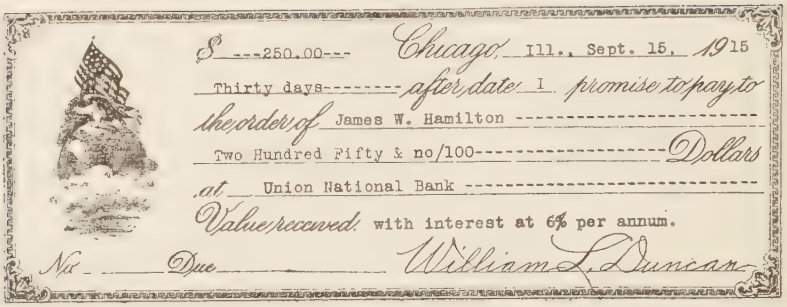
## NOTES

- I. Parties
  - 1. Original
    - a. Maker
    - b. Payee
  - 2. Subsequent
    - a. Indorsers
    - b. Transferrers without Indorsement
    - c. Indorsees
- II. Kinds
  - 1. Payable to Bearer
  - 2. Payable to Order
- III. Forms
  - 1. Ordinary
  - 2. Special
    - a. Judgment Notes
    - b. Collateral Notes
- IV. Special Matters
  - 1. Accommodation Parties
  - 2. Incomplete Instruments

**165. Definition.** A negotiable promissory note is a written promise by one person to pay to some other person therein named, or to his order, or to bearer, a fixed sum of money, at all events, and at a time specified therein or at a definite time which must certainly arrive. To be negotiable a note must also possess all the essential elements of negotiable paper.

**166. Parties.** There are two original parties to a note. The *maker* is the one who signs it, agreeing to pay it. The *payee* is the one to whom, or to whose order, it is made payable. In the note above, William L. Duncan is the maker and James W. Hamilton is the payee. The maker of a note may make it payable to himself or order, but this requires that it be indorsed by him, that is, that he again write his name across the back, before it can be put into circulation.

## Form of Note


$ ---250.00--- Chicago, Ill., Sept. 15, 1915
Thirty days--------after date I promise to pay to
the order of James W. Hamilton
Two Hundred Fifty & no/100----------Dollars
at Union National Bank
Value received. with interest at 6% per annum.
No. Due William L. Duncan

**167. Joint and Several Notes.** A note which is signed by a single maker is a several note, for he alone is liable. When more than one name appear as signatures on the face of the note, that is, when there are two or more makers, the question arises as to whether there is a several promise by each or only a joint promise by all. This is the same question that arises under joint and several contracts, previously discussed in the chapter on Contracts. If the note be drawn, "We promise to pay, etc.," and is signed by two or more parties, it is a joint note. A note signed by more than one person and beginning, "I promise," or "We or either of us promise," is several as well as joint. In a joint and several note the holder can sue all the makers together, or he may sue them separately, for in such a note each assumes the entire responsibility for paying the entire sum. If the note be joint only, all the makers must be sued together. At common law it is well settled that if one of the joint makers dies, his estate is discharged, and the survivor, or survivors alone, can be sued. This is not true in the case of a joint and several note. Statutes in some states have changed this rule, so that even by a joint note the estate of the deceased is bound, while others have accomplished the same result by abolishing all distinctions between joint and several notes, making all obligations signed by two or more parties, joint and several. (See Section 26.)

**168. Essentials.** While in commercial usage it is customary to print forms for notes with the words "value received," and to make them payable at a bank, neither of these things is necessary

to impart negotiability, according to the N. I. L., and according to the rules of a majority of the states which have not adopted the uniform act. A note in the following form possesses every requirement essential to its negotiability:

| | |
|---|---|
| *$100.00* | ST. LOUIS, MO., *Sept. 20, 1915.* |
| *One year* AFTER DATE *I* PROMISE TO PAY | |
| TO THE ORDER OF *William Sampson* | |
| THE SUM OF *One hundred and no/100* DOLLARS. | |
| *Casper Whiting.* | |

It is payable absolutely, within a specified time, in money, to a person named, and is an instrument in writing with words of negotiability. Provisions for the payment of interest, statements of the consideration, place of payment, and even a provision that the maker agrees to pay a reasonable attorney's fee in case collection be made by suit, can be added.

In some states where the N. I. L. has not been adopted the addition of a provision regarding attorney's fees, or of a seal after the name of the maker, is held to destroy the negotiability of the instrument.

**169. Transferability.** Negotiable notes may be transferred by indorsement the same as accepted drafts. The payee becomes the first indorser. Subsequent parties who acquire rights in the note by indorsement and delivery or delivery without endorsement may also become indorsers by writing their names on the back of the note and transferring it to another. A person who becomes an indorser in this manner also enters into a special contract with the parties who acquire rights under his indorsement, the nature of which contract will be discussed in a later chapter. All notes, except those payable to bearer or indorsed in blank or to bearer, must be indorsed in order to be transferred. If they are delivered by a holder to a subsequent party without indorsement, the latter has a right to demand the indorsement. (Section 49 N. I. L.)

**170. An Accommodation Note** exists when the maker, or one of the makers if the note be joint, has without receiving any consideration signed it for the accommodation of the payee or joint maker, thereby enabling the latter to more readily negotiate it.

The party thus lending his credit is called the accommodation party and is defined by Sec. 36 of N. I. L. as "one who has signed the instrument as maker, drawer, acceptor or indorser, without receiving value therefor, and for the purpose of lending his name to some other person."

The accommodation party is liable to all subsequent holders in due course. If he suffers any loss he may recover from the party whom he accommodated, the latter obviously being unable to enforce the instrument against the one who accommodated him.

**171. Incomplete Notes.** Another way to loan credit, which is sometimes adopted when the exact amount needed cannot be determined at the time the loan is made, is to issue a note in which the space for the amount is left blank, the payee being given authority to fill in the blank up to a specified amount. Issuing such notes is an extremely dangerous practice, and should be avoided because the authority given may be exceeded, and if the note then passes into the hands of a holder in due course the maker will have to pay it, even though at great loss.

EXAMPLE

Ames gave Bates a note in which the space for the amount was left blank, with the understanding that Bates would buy between $400.00 and $500.00 worth of goods, filling in the amount when his purchase was completed. Bates bought from Call $1,000.00 worth of goods, filled in the amount $1,000.00, and endorsed the note to Call. Call sued Ames and collected $1,000.00, as Ames was not able to show that Call knew of the restriction that Ames had placed upon Bates.

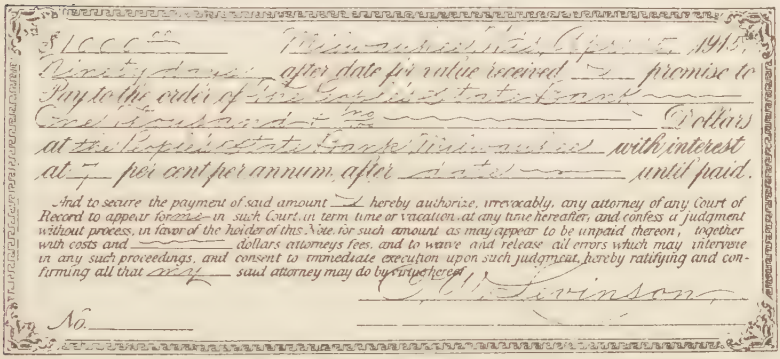
**172.** Frequently the date of payment and the name of the payee are left blank. The rule of the Law Merchant, which has been adopted by the N. I. L., is that any holder has the right to fill in these blanks so as to make a complete instrument, provided the note was actually delivered.

**173. Judgment Note.** A judgment note is an ordinary note to which is added a "power of attorney," enabling the holder to secure a judgment for the amount due (and frequently, at any

time, regardless of the maturity of the note) without the preliminary steps of serving a summons and having a trial.* By including this added provision the maker waives his right to be heard in court before the entry of the judgment. The advantages of such a note are with the holder.

To this "power of attorney to confess judgment," as it is called, are generally added (1) a waiver of exemption laws, and (2) a stipulation for the addition of attorney's fees. As we have seen, not all of the property of a debtor is subject to levy under an execution to enforce a judgment, by virtue of the

**Judgment Note**


$1000 — Minneapolis, Minn. June 1, 1915.
Ninety days after date for value received I promise to
Pay to the order of The Central Trust Company
One thousand — No/100 Dollars
at the Hopkins State Bank Minneapolis with interest
at 7 per cent per annum after date until paid.
And to secure the payment of said amount I hereby authorize, irrevocably, any attorney of any Court of Record to appear for me in such Court, in term time or vacation, at any time hereafter, and confess a judgment without process, in favor of the holder of this Note, for such amount as may appear to be unpaid thereon, together with costs and ——— dollars attorneys fees, and to waive and release all errors which may intervene in any such proceedings, and consent to immediate execution upon such judgment, hereby ratifying and confirming all that said attorney may do by virtue hereof.
C. L. Swinson
No. ———

exemption laws of the several states. The right to such exemptions is usually waived in a judgment note. In the typical form of note printed below there is also a provision permitting a five per cent addition to the judgment for an attorney's fee.

It was originally supposed that the addition of these conditions made the instrument lose its character of negotiability and become nothing more than a contract, but it is now well settled in most states that such notes are negotiable, and they are recognized as such by the N. I. L. If, however, the authorization be to bring suit before maturity, the note is made non-negotiable because the time of payment is then made uncertain.

The advantage of such notes is that it is unnecessary to sue upon them in the ordinary way, in order to secure a judgment. No summons is necessary,

* A "power of attorney" is a legal instrument empowering the person named in it to act as the attorney of the person signing it, in certain specified matters or in all matters of a kind indicated. In this case, the holder of the "power of attorney" is given authority to go into court as a lawyer for the debtor and admit the claim, or "confess judgment" for him.

and while an ordinary suit upon a note requires considerable time between its commencement and the judgment, the entire proceedings of taking judgment on a judgment note may take only a fraction of a day.

**174. Collateral Note.** Notes secured by the deposit of securities, such as stocks, bonds, or mortgages, which are described in the note itself, are called collateral notes. It frequently happens that a banker lending money on a note will require such a pledge for its payment. Read the note carefully. Observe that it contains all that any note contains, and in addition contains stipulations as to the confession of judgment, and the sale of the collaterals. If the amount received from the sale is more than enough to satisfy the debt and the cost of the judgment, the excess should be turned over to the debtor. The negotiability of such notes has not been very generally recognized until the adoption of the N. I. L., which recognizes them as negotiable instruments.

**Collateral Note**

$1500.00 Milwaukee, Wis., May 16, 1916

Sixty days after date for value received I promise to pay to the order of The People's State Bank of Lancaster, Wis. One Thousand Five Hundred —— Dollars, at Milwaukee, Wis. with interest at the rate of 7 per cent. per annum, after due, having deposited with the legal holder hereof as collateral security Two Thousand Dollars Twenty shares of Common Stock of the Union Traction Company of Milwaukee of the par value of Two Thousand dollars represented by certificate #625.

and I hereby give the said legal holder, his, her or their assign or assigns, authority to sell the same, or any part thereof, on the maturity of this Note, or at any time thereafter, or before, in the event of said security depreciating in value, at public or private sale, without advertising the same, or demanding payment, or giving notice, and to apply so much of the proceeds thereof to the payment of this Note, as may be necessary to pay the same, with all interest due thereon, and also to the payment of all expenses attending the sale of the said collaterals, and in case the proceeds of the sale of the same shall not cover the principal, interest and expenses I promise to pay the deficiency forthwith after such sale, with interest at 7 per cent. per annum. And it is hereby agreed and understood that if recourse is had to said collateral, any money realized on sale thereof in excess of the amount due upon this Note shall be applicable to the payment of any other note or claim which the said legal holder may have against me and in case of any exchange of, or addition to the collateral above named, the provisions of this Note shall extend to such new or additional collateral.

C. E. Stevens (SEAL)

(SEAL)

The above is called a "short form" of collateral note. Many collateral notes are much longer, containing more provisions, all stated at greater length.

## REVIEW QUESTIONS

1. Johnson induced Ebert, a German unable to read and write English, to sign an instrument which was in form a promissory note, representing to Ebert that it was a contract appointing him agent to sell patented farm machinery. Johnson completed the note and transferred it to Walker, who paid value and knew nothing of the transaction. Walker sues Ebert on the note. Can he recover? Why?

2. Who is liable on the following promissory note? In what manner? Why?

*$400.00* RIPON, WIS., *Nov. 4, 1915.*

*Thirty days* AFTER DATE *I* PROMISE TO PAY

*Putnam C. Dart*, OR ORDER,

*Four hundred and no/100* DOLLARS

WITH INTEREST AT THE RATE OF *6%* *per annum.*

*J. C. Sherwood,*

*Wm. C. Sherwood.*

3. Is the following a negotiable promissory note? Why?

*$1600.00* *Chicago, Ill., Nov. 4, 1914.*

*When sixty days after this date have elapsed, I, the undersigned, William Day, agree and promise that I will upon the demand of Ernest Young, pay to him, the said Ernest Young, the sum of Sixteen Hundred Dollars, in lawful coin of the realm.*

*William Day.*

4. At the request of Hines, Smith signed a note with Hines for $300, in favor of Carter, without receiving anything for so doing, in order to aid Hines in borrowing the money. Hines signed the note first, Smith placing his name just below that of Hines. If Smith is forced to pay, can he recover from Hines? Why? If Hines pays, can he recover from Smith? Why? From whom may Carter collect? If Carter endorses to Roscoe, from whom may Roscoe collect?

VI

# CHAPTER XVII

## HOLDER IN DUE COURSE

- I. Conditions Necessary
  - 1. Transfer for Value
  - 2. Transfer to an Innocent Holder
  - 3. Transfer in the Usual Course of Business
  - 4. Transfer before Maturity
- II. Rights
  - 1. Subject to Defenses of
    - a. Incapacity of Parties
    - b. Void Instruments
    - c. Alteration or Forgery
  - 2. Not Subject to Defenses of
    - a. Fraud
    - b. Lack or Failure of Consideration
    - c. Illegality
    - d. Payment to Prior Party
    - e. Set-offs

### CONDITIONS OF TRANSFER

**175. Required Conditions.** To be fully negotiable, a paper must be transferred, (1) for value; (2) to an innocent holder; (3) in the usual course of business; and (4) before maturity. Unless all of these conditions attend the transfer of a negotiable instrument, the new holder takes only the rights which he would have taken had the document been a mere contract. If these four conditions are all complied with, the new holder is called, by the N. I. L., a *holder in due course.*

**176. Transfer for Value.** No one can become a holder in due course unless he has paid value for the instrument which is transferred to him. The consideration, or value, which he must pay need not be money, but must be something which the law treats as having value. It may be cash, goods given, liabilities incurred, or rights surrendered. A finder of lost paper is not a holder in due course and cannot enforce it against the defenses

which might have been urged against a prior holder. The same thing is true of one who receives such paper as a gift.

Prior to the adoption of the N. I. L., there was much difference of opinion as to whether taking a note in payment of, or on account of, a pre-existing debt, constituted the giving of value. Section 25 of the N. I. L. states the rule as follows: "Value is any consideration sufficient to support a simple contract. An antecedent or pre-existing debt constitutes value, and is deemed such whether the instrument is payable on demand or at a future time."

EXAMPLES

1. Parsont, induced by Brown's fraudulent misrepresentations, issued a check to Brown as payee. Brown indorsed it to Rosenthal as a loan. When Rosenthal sued Parsont the defense was made that the note had been induced by fraud and that Rosenthal occupied the same position as Brown, the payee. The court refused to allow recovery, stating that Rosenthal had not paid value, and so was subject to the same defenses as Brown would have been. Rosenthal vs. Parsont, 110 N. Y. Supp. 223.

2. A bank canceled a certificate of deposit and credited the amount to the account of the depositor. The question later arose as to whether the bank was holder in due course, and the court declared that this transaction did not constitute the giving of value, being a mere readjustment of the account of the depositor. Commercial National Bank vs. State Bank, 132 Iowa 706.

**177. Transfer to an Innocent Holder.** To be a holder in due course, one must not only have paid value, but he must have received the paper without knowledge, or notice, of any defects in the seller's title, or right to enforce it. If he accepts the paper, paying value for it and yet knowing that the seller's title is defective, or that there is a valid defense to the instrument, he is not an innocent holder; he takes only the seller's title, and no better.

Nor can a buyer of paper deliberately close his ear to any suggestions of fraud or defects in the seller's title, for if he receives any suggestions or if the circumstances are such as would arouse the suspicions of an ordinarily prudent man, he is charged with the duty of investigating before buying.

EXAMPLES

1. A note was drawn by A, payable to himself, and by him indorsed and given to B to sell for cash and to return the proceeds to A, is invalid in the hands of C, who knowing the facts and conditions of B's possession of the

note, took the note from B in satisfaction of a debt due from B to C. Bruggestadt vs. Ludwig, 184 Ill. 24.

2. A gave to B a demand note payable to B or order with the understanding that it should not be negotiated. B, however, indorsed the note for value to C. Afterwards A paid B the amount of the note, supposing that he had retained the note. Later C sued A, and A was compelled to pay him because he was a holder in due course and had known nothing of A's payment to B Nash vs. DeFreville, 2 Q. B. (Eng. 1900) 72.

**178. Transfer in the Usual Course of Business.** A third condition is that the holder must acquire the paper in the usual course of business. By this is meant that it must come as a regular transfer according to the custom of commercial transactions. Thus a receiver or assignee appointed by a court to take charge of an insolvent person's business, who comes into possession of a bill or note, by virtue of his appointment, does not get it in the regular course of business, nor do those who acquire title through him get it in the usual course of business.

EXAMPLE

A trustee in bankruptcy found a note among the bankrupt's assets. This he sold to a third party, who claimed that although the note could not have been enforced by the bankrupt, the transfer to him had made him a holder in due course and that he took title free from defects. He was denied recovery, however, as not having received the paper in the usual course of business. Conley vs. Nelin, 128 S. W. (Tex.) 424.

One who takes a note or bill as collateral security, that is, to secure the performance of some other obligation, is considered under the N. I. L., and by a majority of states that have not adopted the uniform statute, to have taken it in the usual course of business. One who has taken paper as collateral, however, can recover upon it only to the amount of the loss which he suffers on the original debt which it is taken to secure.

**179. Transfer before Maturity.** He who takes paper after maturity, simply takes the rights of the prior holder. If the prior holder's right and title are good, so will his be, but if there are any defenses against his transferrer's right and title, they can also be raised against him. Thus if a thief steals a note after maturity and sells it for value, the taker will acquire no title whatever, as the thief had none to convey. Or, if the maker of a note pays it at maturity, and it is set in circulation

again, accidentally, without the fault of the maker, he will be able to resist another payment of the same obligation even though the paper has passed into the hands of an innocent holder for value.

EXAMPLE

A note provided that any delinquency in the payment of interest "shall cause the whole note to become due and collectible immediately." The note was for five years, but the interest was not paid the first year, and the second year a third party bought it. The court declared that he could not thereby become a holder in due course, because by reason of the additional provision the note had become due and he had purchased it after maturity. Hodge vs. Wallace, 129 Wis. 84.

**180. Holder after Holder in Due Course.** Although the paper, while in the hands of the original holder, may have had many defects and been subject to many defenses, yet when it has once passed through the hands of a holder in due course it is freed of these imperfections. After such a holder in due course has possessed it, any party claiming under him takes the rights, not of the original holder, but of the first holder in due course. Consequently, a holder subsequent to a holder in due course may take paper with knowledge of defenses which might have been urged against an original party and yet not take his rights subject to such defenses. If, however, such a subsequent holder had been a party to a fraud or illegal transaction whereby the note was originally secured he could not escape on the ground of the intervention of a holder in due course.

EXAMPLES

1. B buys a horse, giving a note in payment, and finds that fraud was practised on him in the sale, so that had he paid cash he could have rescinded the purchase and demanded the return of his money. The note, however, has passed from the fraudulent seller of the horse to C, a holder in due course. A, who knows of the original fraud, but was not a party to it, buys the note in due course from C. By so doing, A acquires the title which C had as a holder in due course, although he could not himself have purchased the note from the original seller so as to have become a holder in due course. The reason for this exception to the rule that the holder should be innocent is that C's rights as an innocent holder to negotiate the instrument must be fully protected.

2. The payee of a note, whose title was defective, sold it to a holder in due course and then repurchased it, claiming to be entitled to take the note free from defects because of the intervention of a holder in due course. This

he could not do, because his title is determined as of the time when he first became a party to the note. Andrews vs. Robertson, 111. Wis. 334.

**181. When Paper Matures.** The exact date of maturity is always an important fact, and one about which there should be no opportunity for dispute, for upon this date the rights of a subsequent holder frequently depend. When the time of a bill or note is stated in days, the actual number of days are counted, excluding the day of issue; when it is stated in months, calendar months are understood as the measure of maturity. The maker has the whole of the business day on which the paper falls due to make payment. By the N. I. L., Section 85, the time of payment, or maturity, is further specified as follows:

"When the day of maturity falls upon Sunday, or a holiday, the instrument is payable on the next succeeding business day. Instruments falling due on Saturday are to be presented for payment on the next succeeding business day, except that instruments payable on demand may, at the option of the holder, be presented for payment before twelve o'clock noon on Saturday when that entire day is not a holiday."

**182. Consideration.** So long as the immediate parties to negotiable paper are the only ones interested in it, there must be consideration, the same as in any contract. While the existence of the paper, drawn in negotiable form, presumes that a consideration was given for it, this presumption may be defeated by proof to the contrary between the maker or drawer, and the payee.

If the paper has been transferred to a holder in due course, the absence or failure of consideration will not prevent him from recovering upon it in accordance with its terms. A common practice is to insert the words "value received," in a bill or note, although this is not required by the N. I. L., or by a majority of the states.

The N. I. L., Section 25, states the law regarding consideration, as follows:

"Absence or failure of consideration is a matter of defense as against any person not a holder in due course."

**183. Defenses.** The defenses which may be urged against negotiable paper are of two kinds: (1) Real, or absolute, defenses; and (2), Equities, or personal defenses.

**184. Real Defenses** are those which attach to the instrument itself, and which are good against all persons, regardless of whether or not they are holders in due course. Such defenses exist in case the note or bill is defective because of (1), incapacity of the parties; (2) illegality by statute; and (3) alteration or forgery of the instrument.

*Incapacity of a party* renders him incapable of making an ordinary contract which can be enforced against him, and the same rule applies to negotiable paper. Such a party may indorse a note or bill so as to transfer it, but he does not thereby become liable on any of the special contracts which the Law Merchant implies. He cannot be sued as drawer, maker, or indorser.

*Void instruments* are not enforceable, even by a holder in due course. For instance, a note bearing a higher rate of interest than is allowed by law cannot be enforced by any party, in states where the effect of usury is to make the note void. In some states contracts made on Sunday are void, and where this is true a note made on Sunday would be void even in the hands of a holder in due course.

Alteration of an instrument as contrasted to the forgery of a signature consists in the changing of some material term without the consent of prior parties. Thus it not infrequently happens that the amount, date of payment or rate of interest is fraudulently altered. At common law a material alteration which changed the nature of the original obligation became an absolute defense to any action on the altered instrument no matter who brought the action. This rule is still in force in states which have not adopted the N. I. L. In other states, however, the N. I. L. in Section 124 provides that such an instrument may be enforced by a holder in due course according to its original form before alteration.

The only instance in which the obligation of a prior party may be changed by alteration without his consent is where the active negligence of the party has contributed to the alteration. Courts are not agreed on what this negligence must consist in. It is good business practice, however, never to leave any blank spaces in an instrument.

If the signature of a party is a forgery such party is not liable thereon whether he be a maker, payee, drawer, acceptor or indorser. This is because no one can be made liable for an obligation which he has never assumed.

An alteration may be ratified by the party injured, by his agreement to pay the bill or note in accordance with its terms. This ratification may be made by express promise, whether written or oral, and may even be implied when another has, with reasonable cause, relied on the apparent ratification, to his injury.

**185. Personal Defenses** are those which can be urged against those directly responsible for the injuries claimed, and others whose title is no better, but which cannot be urged against a holder in due course. Such defenses are: (1) Fraud in the transaction; (2) lack, or failure, of consideration; (3) illegality which does not render the instrument void; (4) payment, or cancellation before maturity, and (5) set-offs as against a prior party.

*Fraud* in the transaction in which a paper was issued, if the paper has been delivered, is a defense which cannot be urged against a holder in due course. Thus, if a person is induced to give his note for a specified amount in payment for a horse which he later discovers is not as represented, he may have a defense against the person practicing the fraud and others who have come into possession of the instrument with no better title, but not against a holder in due course.

If, however, the instrument was never delivered as a negotiable bill or note, but by fraud was later made into one, this constitutes a defense on the part of the supposed maker against any person. Such a case may occur when one who is blind or infirm signs a paper by mistake, supposing it to be an ordinary contract, whereas it proves to be a negotiable instrument; or when one signs his name to a blank paper which is later filled in without authority. In neither instance is the instrument actually delivered as a bill or note, and the fraud may therefore be a defense against any holder.

*Lack, and failure, of consideration* are matters of personal defense which can be urged by way of set-off or counterclaim, against all persons not holders in due course. If as between the original parties the instrument was executed as a gift, it cannot be enforced by the party to whom it was given, because of lack of consideration; but it can be enforced by a holder in due course. Conversely, if a paper was given for an apparent consideration,

as for services to be performed, which consideration subsequently fails (as when the party agreeing to perform the services refuses to do so), defense may be made against the original party, or any person claiming merely his rights, to the amount to which the consideration has failed; but this defense cannot be urged against a holder in due course.

*Illegality*, when not such as is declared by statute to make an instrument completely void, can be urged only against the immediate parties, and not against holders in due course. Thus, when a note is given as part of an agreement in restraint of trade, or for a gambling debt, it is not collectible as between the immediate parties, but can be enforced by a holder in due course.

*Payment to prior party.* Payment before maturity discharges the maker's obligation towards the party paid, but if the negotiable instrument is not surrendered to the maker or drawer and destroyed it may still pass into the hands of a holder in due course at any time before maturity, and if it does such a holder can compel payment again.

The careful business man, paying his obligations on bills and notes, requires the party whom he pays to surrender the negotiable instrument when payment is made, whether it be before or after maturity.

**186. Set-offs and counterclaims** have been fully treated under the subject of contracts. Even though the maker of a negotiable instrument may have such a right against the first holder, this right is not effective against a subsequent holder if such subsequent holder be a holder in due course.

**187. Recapitulation.** Negotiable paper, being a substitute for money, is accorded the fullest measure of protection possible by law, so that one who takes it as a holder in due course may feel reasonably safe in accepting it. If the paper is made out in proper form, and is not yet due, the only conditions which a buyer of the paper need inquire into are the credit of the maker and the genuineness of his signature.

When the instrument has passed into the hands of a holder in due course the maker loses practically all of his possible defenses. Often it seems a hardship thus to restrict an original party in his defenses, but as between two parties, the more innocent should be protected, and he who has made possible the existence of the

wrong should bear the consequences. If it were otherwise, negotiable paper would have little value as an aid to business, and the exchange of goods by means of such instruments of credit would be very limited.

## REVIEW QUESTIONS

1. Davies made a note payable to Sandal, or order, due on November 13. The note was not paid at maturity. Some weeks later Davies paid the amount to Sandal but did not receive the note from him. Sandal then transferred the note to Brown, who paid value and had no notice of the maker's payment. What are Brown's rights? Why? Davies rights? Why?

2. Clark, a person to whom a note had been indorsed, and who received the note in good faith and for value, sued Johnson, the maker. This note had been made payable to Bush, but was not completed as to amount, and had been snatched away from Johnson by Bush, without any intentional delivery on the part of Johnson, and indorsed by Bush to Clark. What are Clark's rights? Why?

3. A issues to B a check for $100, payable to B or order, and drawn upon the Peoples' National Bank of Bloomington, Ill. B indorses the check to C, who pays value, and who then raises the amount from $100 to $1000, and indorses it to D, who is a holder in due course. D takes the check to the bank, and receives the money. What are the rights of the bank against A? B? C? D?

4. Ames gave Bates his promissory note for $5000, Bates agreeing that he would in consideration of this deliver to Ames certain bank stock. This he failed to do, but transferred the note to Call, a holder in due course. Call presented the note as a gift to Dale, who sued Ames. What are Dale's and Ames' rights?

5. A stranger asked Jonas, a farmer, with whom he stopped for dinner, to cash a note for $25.00, due in ten days, payable to the stranger, and signed by Burnham, a neighboring farmer. Jonas produced a hundred dollar bill, which was all he had, whereupon the stranger said, "Give me that, and I'll just change these figures to $100 in this note." This he did and Jonas gave him the hundred dollars. When the ten days had elapsed he sued Burnham on the note for $100. What are his rights?

6. Suppose in Example 5 that Jonas had before maturity sold and indorsed the note to Welcome, a holder in due course. Would Welcome's rights have been different from those of Jonas? Why?

CHAPTER XVIII

## TRANSFER

- I. By Delivery
  - 1. When Payable to Bearer
  - 2. When Already Indorsed in Blank
- II. By Indorsement and Delivery
  - 1. Requisites
    - a. Written on Instrument
    - b. Order to Pay Transferee
    - c. Order to Pay Entire Sum
    - d. Accompanied by Delivery
  - 2. Kinds
    - a. In Full
    - b. In Blank
    - c. Restrictive
    - d. Qualified
    - e. Conditional
    - f. Irregular

- I. Conditional Liability
- II. Warranties
  - 1. Instrument is Genuine
  - 2. Instrument is Valid
  - 3. Prior Parties are Competent
  - 4. His Own Title is Good

**188. Transfer by Delivery without Indorsement.** One type of negotiable paper only, viz., that payable *to bearer*, may be transferred by delivery alone. When paper is payable to bearer, no further act beyond delivery is necessary on the part of the transferrer to give to a holder full rights in due course. This delivery must be voluntary.

Delivery may be voluntary or involuntary. When the transfer is made in the usual course of business with the intention to transfer title to the instrument, and the rights thereby rep-

resented, the delivery is voluntary and passes the full rights represented by the negotiable paper. When, however, the paper is transferred by theft or finding, the delivery is involuntary. The thief or finder cannot enforce the rights represented by the instrument, but an innocent purchaser from him can.

EXAMPLE

Hays brought suit on a note payable to bearer, of which Hathorn was the maker. Hays produced the note in court and proved Hathorn's signature. Hathorn then attempted to show that the note had been stolen from him although he did not claim that Hays was the thief. This was not a sufficient defense. Hays vs. Hathorn, 74 N. Y. 486.

**189. Transfer by Indorsement and Delivery.** The only manner in which negotiable paper, other than that payable to bearer, can be transferred so as to create in the new owner the rights of a holder in due course, is by indorsement. Popularly speaking, indorsement consists in the writing by the payee, or the holder, of negotiable paper, of his name on the back of the instrument, and the delivery of the paper so indorsed to a new and subsequent holder. But an indorsement is more than this, in that it must conform to four requirements. These are that it must be (1) in writing, by the payee, on the instrument itself; (2) an order, express or implied, to pay the person to whom the paper is transferred; (3) an order directing payment of the whole sum due on the face of the paper; and (4) accompanied by delivery.

An indorsement on a separate paper is insufficient. The indorsement must be written, though this includes writing with either pencil or ink and also stamping or printing the signature of the person so transferring the instrument, who is called the *indorser*. There must be further, either express or implied, an order to prior parties to pay the sum promised to be paid on the face of the instrument to the person to whom the instrument is transferred, who is called the *indorsee*. In accordance with this rule it is the law in most states that words similar to "I assign the within note," or "I assign all my right, title and interest in and to the within note," are insufficient to constitute the new taker a holder in due course. An assignment is merely the giving of authority to the assignee to collect as on a simple contract; the element of demand upon the maker to pay is missing. A

few states by recent decisions have overlooked this distinction and view a written assignment on the instrument as of the same force and effect as a simple indorsement.*

The law in regard to partial indorsements, as it has always existed in the Law Merchant, is stated in Section 32 of the N. I. L., as follows:

"The indorsement must be an indorsement of the entire instrument. An indorsement which purports to transfer to the indorsee a part only of the amount payable, does not operate as a negotiation of the instrument. But when the instrument has been paid in part, it may be indorsed as to the residue."

The person taking an instrument which has been indorsed in part only, becomes merely the *partial* assignee of a simple contract, and in no wise a holder in due course.

No transfer by indorsement is completed until the instrument has been delivered voluntarily to the new holder.

EXAMPLE

A, payee of a note signed by B, wrote upon it, "Pay to X, (Signed) A," and placed the note in his safe, intending to deliver it in the morning. X broke open the safe during the night and stole the note. As the note had never been delivered to him, he could not enforce it, but if he in turn had transferred it to a holder in due course, the latter could have enforced the note. Greeser vs. Sugarman, 76 N. Y. Supp. 922.

**190. Kinds of Indorsement.** While every indorsement, to be effective to negotiate an instrument, must include the four elements just enumerated, endorsements may be of several kinds. The principal kinds of indorsements are as follows:

1. Indorsement in Full (called a *special* indorsement by the N. I. L.)

Pay to F. F. Judd, or order,
M. K. Jordan.

2. Indorsement in Blank.

P. S. Spangler

* Wisconsin, North Carolina, Minnesota.

3. Restrictive Indorsement.

Pay to Martin McDonald, only.
Samuel K. Levin.

Pay to J. C. Smith, for my use.
A. L. Clarke.

4. Qualified Indorsement.

Pay to J. W. Burke, or order,
without recourse to me.
Allen Moore.

5. Conditional Indorsement.

Pay to A. E. Emmerson, or order,
provided he has reached the age
of twenty-one years,
R. E. Parker

**191. Effect of indorsement.** Before discussing in detail the various kinds of indorsement, the attention of the student is directed to the fact that whenever any of these indorsements is properly made the endorser does three separate and distinct things:

(1) He transfers to the endorsee the right to collect the paper in his own name.

(2) He promises (except in case of a restricted or qualified indorsement) to pay the indorsee if the party primarily respon-

sible fails to do so (provided a proper attempt has been made to collect from the maker, and prompt notice has been given to him, the indorser, of the maker's failure to pay).

(3) He warrants that the instrument is genuine; that he has good title; that the note is not void because of illegality; and that no prior party was incompetent.

If the party primarily responsible fails to pay the instrument when it is properly presented and the indorser is promptly notified of the default, or if any of the indorser's warranties fail, the indorsee may sue the indorser.

**192. An indorsement in full** designates the person to whom the indorser desires to make the instrument payable. It can be paid to no one else, and can be further negotiated only by his indorsement.

The advantage of such an indorsement is that a finder or thief would be compelled to forge the indorsee's name in order to negotiate the instrument further, and when an indorsee's name is thus forged the prior indorser is not liable on his implied contract. The words "or order" are not necessary to an indorsement in full, under the N. I. L.; the phrase, "Pay to (*indorsee's name*)," written over the indorser's signature is sufficient. The indorser may further negotiate the instrument by indorsement in the same manner as though the words, "or order" were present, the reason being that the instrument, having originally been negotiable on its face, will be presumed to continue so unless specifically qualified or limited.

EXAMPLE

May held News' negotiable note. He sold it to Ong. In transferring it to Ong he endorsed it as follows: Pay J. C. Ong, signed L. C. May. What kind of an indorsement was this? Can Ong in turn transfer it by indorsement?

**193. An indorsement in blank** is simply the signature of the indorser written upon the back of the instrument. It is so called because the indorsement proper is left blank, to be filled in by any subsequent holder. Thus if E. C. Becker is the payee or holder of a negotiable instrument he may indorse it by writing his name on the back and delivering it. In such a case the law implies that he has given authority to any subsequent holder to write above his name a direction to the maker or acceptor to pay.

If Arthur Long were the holder he would be authorized to write above Becker's signature the words, "Pay to Arthur Long, or order," making the blank indorsement full.

The effect of indorsing a paper in blank is to make it payable to bearer, because any holder has this implied authority to complete the indorsement. It may, as long as the indorsement continues blank, pass from hand to hand without further indorsement. Blank indorsements are not entirely satisfactory from the view-point of the cautious business man, because if the instrument is stolen or lost, the paper, having the effect of an instrument payable to bearer, may be readily negotiated and pass into the hands of a holder in due course, after which the true owner will be without redress.

**194. Restrictive indorsements** are of three kinds. A restrictive indorsement (Sec. 36, N. I. L.) may be one which either (1) prohibits the further negotiation of the instrument; or (2) constitutes the indorsee the agent of the indorser (as for collection); or (3) places the title to the instrument in the indorsee for him to use for the benefit of some other person.

**195. A Qualified indorsement** is a form of indorsement by which the indorser limits his implied contract with subsequent parties. The usual form is to write such a phrase as, "Pay to G. W. Burke, or order, without recourse to me. Allen Moore." It is sufficient if the words, "Without recourse," alone be written above the signature of the indorser. In this manner the indorser escapes a *portion* of his liability as an indorser. He does not escape his warranty, however, that the prior signatures are genuine, that the note is not invalid for illegality or incompetency of the parties, and that he has a good title.

**196. Conditional indorsement.** When a condition is imposed upon an instrument in connection with an indorsement, it is said to be indorsed conditionally. The legal effect is to limit the negotiable character of the paper as to subsequent parties, and to prevent further negotiation by them until the terms of the condition have been complied with.

The party required to pay an instrument may disregard a condition imposed by an indorser, but the party receiving the money must hold it subject to the rights of the party who indorsed conditionally. (Sec. 69, N. I. L.)

**197. Exceptional Cases.** In connection with the indorsement of a negotiable instrument, it is necessary for the business

man handling commercial paper to understand the effect of three unusual sets of circumstances:

*Blank Indorsement Followed by Full Indorsement.* It has been stated that the indorsement of an instrument in blank has the effect of making the instrument payable to bearer, because any holder has the right to fill in the blank. (If, instead of filling in the blank, a subsequent holder indorses the paper in full, the instrument can then be transferred to another only by indorsement, and not by mere delivery.)

This rule is adopted in Section 30 of the N. I. L., as follows: "An instrument is payable to bearer when the *only* or *last* indorsement is an indorsement in blank."

Morris signs a note payable to bearer and delivers it to Jones, who indorses it "Pay to order of Higgins," and delivers it to Higgins, from whom it is stolen. The thief forges Higgins' name and the note is then transferred to Smith, an innocent holder in due course. Smith may thereupon collect the note from Morris, but has no rights against Jones or Higgins.

*Full Indorsement of a Bearer Note.* A bearer note is transferable by delivery, and it does not lose this characteristic if a holder indorses it in full. It will continue to be transferable by delivery, and will be valid against the maker, though the indorser in full is liable only to those who claim rights in the instrument through and under his indorsement.

*The Indorser's Contract.* It has already been noted that every indorser by his indorsement makes certain warranties and that he contracts with all subsequent parties that he will pay the instrument indorsed if the maker does not; but *this engagement upon his part is conditioned upon proper presentment for payment and prompt notification to him of non-payment.* Each indorser may look to all prior indorsers for satisfaction, in case of loss to himself, because he acquired his rights from or through them.

The contract of warranty applies not only to indorsers but to persons who transfer a bearer instrument by delivery without indorsement for value; the latter, however, cannot be held for payment if the maker fails to pay.

**198. Irregular Indorsers.** An irregular indorser is one who places his name on the paper without being a party to the instrument in the regular chain of title, or without receiving any

consideration for so doing. There was much difference of opinion as to the nature of his liability before the N. I. L., and each state had its own view. The N. I. L., Section 63, declares that such a person is to be deemed an indorser as to all subsequent parties, and assumes the liabilities of an indorser.

EXAMPLE

On the following instrument, Mapes is deemed an indorser.

*$600.00* CHICAGO, ILL., *Nov. 2, 1915.*

*Sixty days* AFTER DATE *I* PROMISE TO PAY

*William E. Stone*, OR ORDER,

*Six Hundred and no/100* DOLLARS,

WITH *6%* INTEREST.

*Edgar Mapes.* (Signed) *Walter A. Call.*

## REVIEW QUESTIONS

1. Inspect the following note:

Chicago, Jan. 18, 1916.

Three years from date I promise to pay to the order of John Gordon, Five Hundred Dollars, with interest at six per cent per annum.

(Signed)
Richard Meyer.

This note was indorsed:

Pay to George Wheeler if my house is completed before the maturity of this note.

(Signed)
John Gordon.

Suppose that at the maturity of this note it is presented for payment to Meyer, who pays Wheeler, and Gordon's house has not been completed. What are Gordon's rights, if any, against Meyer? against Wheeler? Why?

2. Goss, an infant, makes a note for $125, payable to Baldwin, or order, which Baldwin indorses by a full indorsement to Castle, who indorses without recourse to Dawson, who in turn indorses it in blank to Edison. The note

not being paid at maturity, what are Edison's rights, if any, against Goss? against Baldwin? against Castle? against Dawson?

3. Inspect the following draft:

Chicago, June 1, 1916.

Two months after date pay to the order of Call the sum of Five Hundred Dollars, and charge to the account of

To Bates, (Signed)
Cleveland. Ames.

Call indorses this draft in blank and loses it. It is found by Dale, who fills out the blank indorsement to himself, and indorses it without recourse to Evans, a holder in due course. At maturity Bates refuses to pay it. What are Evans' rights against Ames? against Bates? against Call? against Dale?

4. Butler by fraud secures a promissory note payable to his order from Warren. Butler indorses it without recourse to Campbell, a holder in due course, who in turn indorses it in blank to Dore, who knew of the original fraud, but was not a party to it. What are Dore's rights against Warren?

5. If in the above example Warren refuses to pay the note, what are Dore's rights against Butler? against Campbell?

6. (*a*) Write a note embodying the following conditions: Maker is yourself, payee is Harvey Rew, amount is $50, payable sixty days from date. (*b*) Indorse it in full by Rew to Herman Anderson, who indorses it to George Caldwell without recourse, who restrictively indorses so as to be payable only to Samuel Morgan.

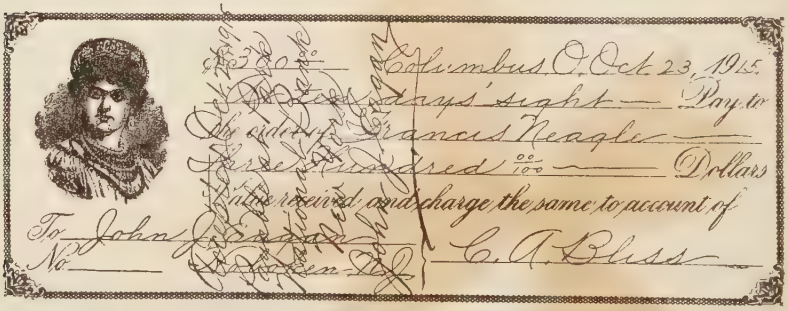
## CHAPTER XIX

## PRESENTMENT FOR ACCEPTANCE

- I. When Necessary
  1. Instruments payable after sight
  2. Express stipulation
  3. Place of payment not drawee's home or business address
- II. Tests of Sufficiency
  1. By whom and to whom made
  2. Place of presentment
  3. Time of presentment
  4. Manner of presentment
- III. Proceedings on dishonor
  1. Notice to prior parties
  2. Protest of foreign drafts

**199. When Presentment for Acceptance is Necessary.** In the chapter entitled "Drafts," the rights and liabilities of the three parties to the instrument have been discussed.

**Accepted Draft**




The three parties in the above draft are Bliss, the drawer; Neagle, the payee; and Eagan, the drawee, who may become the acceptor. By drawing the instrument, the drawer, Bliss, agrees

that he will pay the sum of $300 to Neagle,* or any indorsee subsequent to Neagle, if the drawee does not accept it if properly presented.

The student should carefully distinguish between presentment for payment and presentment for acceptance. Presentment for payment is necessary in connection with all negotiable paper when it is desired to charge those secondarily liable. Presentment for acceptance is a procedure relating only to time drafts.

The drawer's contract is a conditional one, similar to that of an indorser. The payee or his indorsee, however, may lose all rights against the drawer by failure to present the draft for acceptance.

Presentation for acceptance is made to the drawee, and is necessary only in three instances. These are: (1) when the draft is payable after sight, or when from the nature of the promise in the draft, presentation is necessary to fix the date of maturity of the instrument; (2) when it is expressly stipulated in the draft that it shall be presented for acceptance; or (3) when the draft is drawn payable elsewhere than at the residence or place of business of the drawee. In all other cases no presentation for acceptance is necessary, and the drawer may be made liable if the drawee refuses to pay on the presentation of the draft for payment. (N. I. L., Sec. 143.)

**200. Why Presentment is Necessary.** The drawee of negotiable paper is usually under no obligation to accept unless he has agreed to do so, and the holder cannot sue him even though he have funds belonging to the drawer which he refuses to pay, for there is no contract between the payee, or holder, and the drawee. Such suit could be brought by the drawer only. If the drawee refuses to accept and thereby promise to pay, the holder may ordinarily require payment from the drawer. But if the draft is one requiring presentment for acceptance, and such presentment has not been properly made, the holder has failed to perfect his rights against the drawer and has acquired none against the drawee.

* As between drawer and payee, if lack of consideration can be shown the drawer is freed from liability. This would be the case if in the above instance the draft had been given for collection—Neagle would have been merely an agent for Bliss.

**201. By and to Whom a Draft Should be Presented.** The draft should be presented by the lawful holder, or his authorized agent, to the drawee or his authorized agent. The party in possession of the draft is presumed to have the right to present it, and the drawee assumes no unusual risk when he accepts a genuine draft on presentment, that is, he is not required to investigate the holder's right to the instrument. If the draft is drawn on a firm, presentment to any partner is sufficient, but if it is drawn on two drawees, not as partners, it should be presented to both, and if the acceptance of one only is taken, it is at the risk of the holder, unless the one accepting has authority to accept for both. If the drawee cannot be found, inquiry should be made for some person authorized to accept for him, but if acceptance is made by an agent of the drawee, it is necessary for the holder, before he can collect from the drawee, to prove that the agent was authorized to accept. If the drawee is dead, the draft should be protested at once so as to permit charging the drawer.

**202. Where Presentment Should be Made.** Presentment for acceptance should be made either at the drawee's place of business, or at his residence. Even when a draft specifies the place of payment, it should be presented for acceptance, not at that place, but at the office or home of the drawee, for the place of payment is not material until after acceptance. If the drawee has moved, diligent inquiry should be made to ascertain his new residence or place of business, and presentment should be made there. If he cannot be found, the draft should be treated as dishonored.

**203. Time Presentment Should be Made.** Presentment for acceptance should be made within the usual business hours, and except when a bank is the drawee, these usually extend until bed-time. It does not matter when it is made, provided some authorized person is seen and presented with the instrument, though if the hour is an unreasonable one, and no answer is received, the presentment is without legal force and effect.

The draft must be presented within a reasonable time after the holder has received it. If it is not so presented, the drawer will be discharged of all liability, even though he may have suffered no actual damage from the delay. What is a reasonable

time, differs with the circumstances of different cases. In general the holder must act as any ordinarily prudent business man would act. When he receives a draft he must either indorse it to some other person, and so keep it in the process of negotiation, or he must present it for acceptance. The safer course for the business man to adopt is to present promptly all drafts in which presentment for acceptance is required.

If the holder has delayed for an unreasonable time, the drawer is excused from all further liability, unless the holder can show that he was prevented from presenting it because of some lawful excuse, such as sickness, inevitable accident, war, pestilence, or disease. Such excuses, to be valid, must include circumstances which were beyond the holder's control, and which he could not with due diligence have overcome.

**204. How a Draft Should be Presented.** The holder should make an actual exhibit of the draft to the drawee or his agent, and request its acceptance. This is because the drawee's acceptance is properly written across the face of the draft, and unless actually presented this cannot be done. If, however, the person making presentment should describe the draft with sufficient accuracy and no demand should be made for its actual production the exhibition of the draft itself would be waived, and the presentment would be sufficient to hold the drawer liable for the refusal to accept.

Upon presentment the drawee has the right to hold the draft for twenty-four hours, in order to give him time to investigate his financial affairs, and those of the drawer, before deciding whether he will accept or refuse the draft.

**205. Result of Presentment for Acceptance.** The result of a proper and sufficient presentment of a draft for acceptance may be either (1) an acceptance by the drawee; or (2) a refusal to accept, called a *dishonor* of the instrument.

If the drawee accepts in legal form, the elements of which are discussed in the following paragraphs, he becomes liable to the holder and all subsequent parties on a new contract, and the drawer is liable contingently in the event that the acceptor fails to meet his obligations.

If the drawee dishonors the draft, the holder may at once, by appropriate legal proceedings, called *protesting the instrument* and *giving notice of dishonor*, establish his right to collect the amount of the instrument from the drawer.

**206. Proceedings Upon Non-Acceptance.** If instead of accepting the draft by means of one of the forms of general acceptance, after a proper presentation of the instrument has been made to him, the drawee refuses it or neglects to accept it, the draft is said to be *dishonored*, and the holder is at liberty to hold the prior parties liable to pay to him the amount of the draft. He does this by giving immediate notice to all prior parties (the drawer, payee, and previous indorsers) that the draft has been dishonored by the drawee and that they will be held liable to pay it. The holder need not wait for the maturity of the instrument, but may at once collect from all these prior parties who were *conditionally* liable.

If the draft is a *foreign* bill of exchange (See Sec. 144) it should also be protested, and then notices should be sent. (For forms and discussion of protest, see Sec. 219.)

Unless such notices of dishonor are deposited in the mail addressed to the prior parties conditionally liable, or are left at the place of business or residence of the prior parties on the day of or the day following such refusal to accept, they cannot be held liable to pay the instrument to the holder. Notice to all prior parties is ordinarily given by the holder, but may be given by one prior party to another.

EXAMPLE

If Bliss is the drawer; Neagle, the payee and an indorser; Walker, an indorser; and Selden, the holder; and the draft is refused acceptance by the drawee, Eagan; the normal method would be for Selden to give notice of dishonor to Walker, Neagle, and Bliss. It might be, however, that he knew Walker to be reliable and so notified him alone. In this event Neagle and Bliss would be discharged from liability for payment, unless Walker in order to protect himself should give notice to them. This notice would be sufficient to them, and if Walker were forced to pay the draft, he in turn could collect from Neagle, and Neagle from Bliss, each recovering from the party, or parties, named in the draft, or on its back, prior to his own name.

The function of notice of dishonor is to give an opportunity to parties who, because of the refusal of the drawee to accept,

are charged to pay the draft, to protect themselves by appropriate action against either the drawee or parties prior to themselves. The drawee, payee, and indorsers are conditionally liable, and the condition on which their liability to pay the draft depends is that the drawee should on proper presentment refuse to accept it and that they should be given sufficient notice of that refusal.

## REVIEW QUESTIONS

1. A draft payable to order is stolen from the payee. The thief forges the payee's indorsement, and transfers the draft to Holden, a holder in due course, who presents it to the drawee, who accepts it. Holden then transfers it to Rawson who is also a holder in due course. At maturity the acceptor refuses to pay it. What are Rawson's rights? against the acceptor? the payee? the maker? against Holden?

2. Write a draft in which you are the maker; David Davis, the payee; Edgar Evers, the drawee; which requests the drawee to pay the sum of $500 thirty days after sight.

Write the drawee's general acceptance on the draft; also a full indorsement from the payee to Morris Levy; also a blank indorsement by Morris Levy to Benjamin White.

3. Inspect the following draft:

*$750.00* NEW ORLEANS, *Sept. 22, 1916.*

*Two months* AFTER SIGHT, PAY TO

*George Jenkins,* OR ORDER,

*Seven Hundred Fifty and no/100* DOLLARS, AND CHARGE TO THE ACCOUNT OF

To *L. Graves, Tampa, Fla.* *Charles Roberts.*

On September 25, Jenkins presented this to Graves, who wrote across the face the words: "Accepted, Sept. 25, 1916, to pay $700 in cash and $50 by my own note, (Signed) L. Graves." Jenkins then indorsed the draft to Wilfred Munday. Graves failed to pay Munday $750. What rights has Jenkins against Roberts? Why?

4. Suppose that in the above draft Jenkins had gone to Graves' house at two o'clock in the morning with the draft, and that when Graves put his head out of an upper window Jenkins had exhibited the draft and demanded

its acceptance, saying that he had to take an early morning train for Key West. That Graves had told him to "go home where you belong," and had closed the window. What rights would Jenkins then have against Roberts?

5. Inspect the following draft:

Kansas City, Mo., Jan. 22, 1916.

Thirty days from sight pay to Louis Weber, or order, Five Thousand Dollars, and charge to the account of

To Sam Dawson, Vroman Main.
St. Joseph, Mo.

This draft is indorsed on the back as follows:

Louis Weber,
Claude Grundy,
Kent Murray.

On January 25, 1916, Charles Moore, a holder in due course, presented the draft to Dawson, who dishonored it. Moore at once notified Murray and Weber of the dishonor. Weber immediately notified Main. From whom can Moore collect the $5000? from Dawson? from Weber? from Murray? from Grundy? If Weber should have to pay it, would he have any rights? Against whom?

6. Make a draft with imaginary parties which will not need to be presented for acceptance in order to charge the drawer.

7. Ames and Bates signed a note reading, "We or either of us promise to pay to Call $1000." At maturity it was not paid. Name three ways in which Call can bring suit for collection.

8. Windmuller entered into a contract to sell and Pope to buy "about 1200 tons of old iron rails for shipment from Europe at the seller's option at any time from May first to July first at $35 a ton." Before the first of May Pope notified Windmuller that he would not accept any rails under the contract. Was Windmuller entitled to any damages? If so, how much?

9. Smith paid Brown for groceries by giving him an order on Jones, Smith's employer, for $15.00, due thirty days after sight. Jones refused to accept the draft, and two months later Brown sued Smith for the $15.00. Smith had in the meantime left Jones' employ and claimed that in settling with Jones he had allowed the $15.00 Could Brown collect from Smith? Why?

## CHAPTER XX

## PRESENTMENT FOR PAYMENT

The student should carefully distinguish between presentment for acceptance, which has been discussed in the preceding chapter, and presentment for payment, which is the subject of this chapter. Wherever the word *presentment* is used alone in this chapter, it means presentment for payment.

**207. When Presentment for Payment is Necessary.** The *acceptor* of a draft and the *maker* of a note are the parties who are primarily liable, for they have engaged absolutely to pay the paper on the day of its maturity. No formal presentment is necessary to charge either of them, for it is their duty to pay it, and if they fail in this, suit may be brought against them at once. If no place of payment is specified in the instrument, it is the duty of the party primarily liable to seek out the holder and make a tender to him. If a place of payment be designated in the instrument, and the maker or acceptor is ready and willing to pay the instrument at that place, his readiness there amounts to a tender.

On the other hand the contract of the drawer of a draft after acceptance, and of the indorsers of a draft or note, is conditional upon the proper presentment of the instrument to the party primarily liable and his refusal to pay it. Presentment for payment is therefore a preliminary to charging those parties who are secondarily liable, for their contract to pay is conditioned on presentment to the acceptor or maker and his refusal to pay.

**208. By Whom Presentment Should be Made.** Presentment of the instrument for payment must be made by the holder, or by some person authorized to receive payment in his behalf. So far as the acceptor or maker is concerned, payment may be safely made to anyone who appears by the instrument, or its indorsements, to be the legal holder. A presentment by such a person will be sufficient to charge the drawer or indorsers in the event of refusal to pay.

209. **To Whom Presentment Should be Made.** Presentment for payment should be made to the person who is primarily liable on the instrument, or if he is absent or inaccessible, to the person apparently in charge at the place where the presentment is made. If the instrument be a draft the presentment should be made to the acceptor; if a note, to the maker. If the primary liability be joint, the presentment must be made to all makers or acceptors. Should the maker or acceptor be dead, the presentment should be made to his personal representative, who is either the executor or administrator.

210. **Where Presentment Should be Made.** When the paper is payable *generally*, that is, when no place of payment is designated, it should be presented at the place of business of the maker or acceptor, or at his home. If his address be unknown and cannot be discovered, the presence of the instrument in the city named in the hands of the holder or his agent on that day will be sufficient. Presentment is usually made by sending the instrument to some bank for collection. The bank then makes the necessary demand. Under all circumstances, due diligence must be used to find the principal debtor, and present the paper to him, or if a place of payment be specified, to present the instrument at that place, and that place alone.

211. **Time of Presentment.** Presentment must be made on the day of maturity. If made either before, or after, the presentment is insufficient to charge those parties who are secondarily liable.

Not only must the presentment be made on the proper day, but it must be made at a reasonable hour. If the place of presentment be at a business office, the usual business hours of the day form the time limit for presentment; if payable at the maker's or acceptor's home, the limits are the hours of rising and retiring customarily followed in the community.

Presentment is necessary to charge the parties secondarily liable, they having agreed to pay in the event that the maker or acceptor is given a reasonable and proper opportunity to pay, and refuses. It would be unreasonable to call one out of bed at midnight to pay a draft or note, and it would be improper to ask the maker or acceptor to pay before the paper became due. Therefore such a presentment will not be sufficient to throw the responsibility for the maker's or acceptor's refusal upon the drawer or indorsers.

**212. Presentment of Checks.** A check must be presented for payment within a reasonable time after its issue or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay. Checks are drawn on a bank, requiring the bank to pay the payee out of the funds of the drawer on deposit in the bank. The drawer has impliedly promised to pay if the bank fails to do so. His contract is conditioned on the presentment of the check for payment within a proper time, because should the check be outstanding for a long period the bank might become insolvent and fail and the money which he had left there to pay the check might be lost. The rule is designed to cause the payee, who has slept on his rights, to be the loser in such a case, rather than the drawer of the check.

**Reasonable Time.** It is generally considered among business men that twenty-four hours is a reasonable time to hold a check, and that it should be presented for payment, started on its route of collection, or indorsed to another person within that period. Business usage allows each indorser twenty-four hours as a reasonable time in which to dispose of the check.

**213. Drafts Payable on Demand.** The general rule that presentment must be made on the day of maturity does not apply to sight drafts, for the obvious reason that they are matured whenever presented. The only requirement as to them is that they must be presented within a reasonable time or the parties secondarily liable will be discharged. This length of time depends upon business usage. It has already been noted that under the N. I. L. instruments payable "at sight," are treated as payable on demand.

**214. Holidays.** In fixing the period of maturity of negotiable paper, the question as to presentment of paper becoming due on a holiday is often of importance. Each state fixes its own holidays, and negotiable paper becoming due on a legal holiday, as Christmas, Thanksgiving, or New Year's Day, or on a Sunday, is properly presentable the day following, or on the next succeeding business day (except in States where days of grace are still allowed). Thus, when paper falls due on Saturday, the Fourth of July, it is properly presentable on Monday.

**215. Manner of Presentment.** Presentment for payment should be made by an actual exhibition of the paper. This is for the reason that the acceptor or maker has the right to demand that on his payment the instrument should be delivered to him. If the place of payment be at a bank, the presence of the instrument in the bank at maturity, ready to be delivered to any one who may be entitled to it on payment of the amount due, will be sufficient.

Delay in making presentment for payment until after the day of maturity is excused only when the delay is caused by circumstances beyond the control of the holder, and is not due to his fault or misconduct. If there be such delay the holder must prove that it was due to unavoidable circumstances.

**216. Presentment Dispensed With.** Presentment for payment is not necessary in order to charge the drawer or indorsers, (1) when after the exercise of reasonable diligence it is impossible to find the party primarily liable and presentment cannot be made; and (2) when presentment has been expressly or impliedly waived by the parties secondarily liable. A waiver of presentment is made if the indorsers write on the instrument words similar to "Presentment and notice waived," or if they have at or about the time of maturity entered into an agreement with the holder that they will pay the instrument, because of the threatened dishonor by the maker or acceptor. The first is an express waiver; in the second instance the waiver is implied.

**217. The Instrument is Discharged** if, upon presentment for payment, it is paid. The drawer and indorsers are relieved of all further liability, and the instrument itself is usually delivered to the party making payment, or is canceled upon its face, or (usually) both.

**218. When Payment is Refused,** the instrument is said to be dishonored, and the holder's rights against the parties secondarily liable, the drawer or indorsers, become important. If the holder has performed the necessary acts of presentment for payment, and the instrument is dishonored, only one more process remains necessary for him to perform before he can charge the drawer or indorsers with the payment of the instrument. This process is called *protest and notice of dishonor* and is designed to protect

the parties secondarily liable by requiring that they be given notice of the dishonor by a formal method.

**219. A Protest** is a form of solemn declaration written by a notary public to be attached to the instrument, or to a copy of it, stating that he duly presented the note or draft for payment and that it was dishonored. Protest is required in the case of a foreign draft, as distinguished from inland drafts and notes, and is usually made even when not required, because the signed and sealed statement of a notary public is effective evidence that the presentment was properly made and payment refused.

Business usage is for the holder to employ some notary public to make this presentment, and in the event of dishonor, to make, on the day of the dishonor, a certificate of protest of the instrument. The protest is usually written on a blank form and enumerates the following facts: (1) Time of presentment; (2) Place of presentment; (3) Fact of, manner of, and reason for presentment; (4) Fact that payment was demanded; (5) Fact of dishonor; (6) Name of party to whom presented; (7) Name of party by whom presented; (8) Copy of the instrument presented, attached to protest.

### Certificate of Protest

*State of Illinois,* }
*Cook County,* } *ss.*

**Be it Known,** *That on this 30th day of January, in the year of our Lord one thousand nine hundred and sixteen, I, E. J. Hoskins, a Notary Public, duly commissioned and sworn, and residing in the City of Chicago, in said County and State, at the request of W. F. Cadwell, went with the original note, a copy of which is hereto attached, to the office of Oscar E. Bartlett, and demanded payment thereon, which was refused.*

*Whereupon I, the said Notary, at the request of the aforesaid, did* **Protest,** *and by these Presents, do* **Solemnly Protest,** *as well against the maker of said note and the endorsers thereof, as all others whom it may or doth concern, for exchange, re-exchange, and all costs, charges, damages, and interest already incurred by reason of the non-payment of the said note.*

*And I, the said Notary, do hereby certify that on the same day and year above written, within forty-eight hours from the time of such protest, due notice of the foregoing Protest was put in the Postoffice at Chicago, Ill. as follows: Notice for Samuel H. Phillips, Ottawa, Ill., notice for Harry Watkins, LaGrange, Ill., notice for M. J. Morris, Chicago, Ill. Each of the above named places being the reputed place of residence of the person to whom this notice was directed.*

(Place for Seal.)

**In Testimony Whereof,** *I have hereunto set my hand and affixed my Official Seal, the day and year first above written.* E. J. HOSKINS, *Notary Public.*

This certificate, being executed by an official of the state, is evidence that the proper presentment was made, and if any question is raised about the presentment it may be shown to the court, making it unnecessary to produce further witnesses.

**220. Notice of Dishonor.** The holder of dishonored paper, whether he protests the paper or not,* must always send notice of the dishonor to all prior indorsers whom he wishes to hold, the notice being a statement of the fact of dishonor and of an intention to hold liable the party notified. The notice should be presented or mailed within twenty-four hours after the dishonor. This promptness is necessary in order to give the parties secondarily liable sufficient opportunity to protect themselves by appropriate steps against the party primarily liable, who dishonored the instrument, and against other parties secondarily liable.

**Notice of Protest**

Notice of Protest of Note.

State of Illinois, }
County of Cook } ss.

Chicago Jan. 30 1916

Sir:— A note for $500.00

Dated Jan. 30, 1915
Payable Jan. 30, 1916
Signed by Oscar E. Bartlett
Endorsed by Samuel H. Phillips
Harry W. Atkins & M. J. Morris

Being this day due and unpaid, and by me PROTESTED for non-payment, I hereby notify you that the payment thereof has been duly demanded, and that the holders look to you for payment. Damages, interest and costs.

Done at the request of W. F. Caldwell, the holder

E. J. Hoskins
Notary Public

To Samuel H. Phillips,
Ottawa, Ill.

When a notary is employed to protest a note or draft, he usually also mails notices of dishonor, and his fees, which are specified by law, are added to the amount to be paid by the indorser, drawer, or maker.

**221. If Notice be Waived** by a party secondarily liable, as described in Sec. 216, neither protest nor notice is required to charge him with liability.

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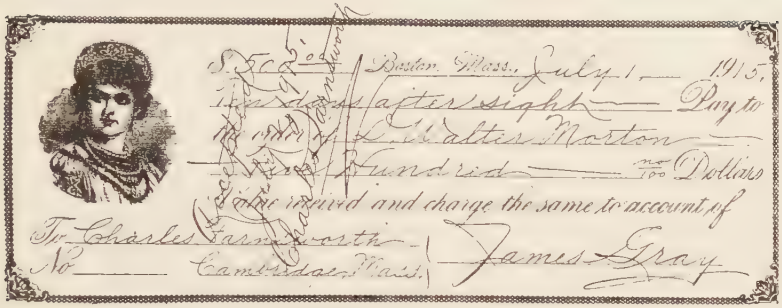
* Notice of dishonor is *always* required, to hold the parties secondarily liable. (Protest is always desirable, but is not required by law in case of inland bills, though it is required in case of foreign bills.)

## REVIEW QUESTIONS

1. Inspect the following draft:


$ 5 C 2 0 0
Boston, Mass. July 1 1915
after sight Pay to
Walter Morton
Two Hundred no/100 Dollars
value received and charge the same to account of
To Charles Farnsworth
No Cambridge, Mass.
James Gray

This draft was presented for payment by Morton to Farnsworth at his home in Cambridge, at nine o'clock in the evening of July 12, and Farnsworth, who had retired for the night, put his head out of an upper story window and told Morton to go home and keep still. Morton immediately sent notice of dishonor to Gray, who claimed to have been discharged because of an improper presentment. Was Gray right? Why?

2. The Victoria Hotel Company was an indorser of a draft which had been dishonored. The holder sent a notice of dishonor to the hotel by a messenger boy, who left the notice at the cashier's window, but failed to call the attention of anyone to it. Was this notice sufficient so that the hotel company could be held liable to pay the instrument as an indorser? Why?

3. A gives his note to B payable in wheat. C innocently purchases the note from B for value before maturity, and in the usual course of business, but at maturity A refuses payment, claiming that the paper was secured without consideration. Can C collect it from A?

4. A secures B's note without consideration and indorses it before maturity and for value to C, who has knowledge of the lack of consideration. Can C collect it from B?

5. In the above case, suppose C purchased the paper innocently before maturity and for value, and then transferred it to D, who had knowledge of the lack of consideration between A and B. Could D collect it from B?

6. What would be your answer to No. 5, provided the sale from C to D was after maturity?

7. A playfully writes his name on a blank paper and hands it to B. B fills out a promissory note above it and at once sells it to C, who knows nothing of the deception practiced by B. Can C collect it from A?

8. A owing B $100 writes and signs a promissory note for that amount, payable to B or bearer, intending to deliver it next day. A locks the paper in his safe, but in the night a burglar breaks open the safe, gets the note and sells it to C, an innocent purchaser, for value and before maturity. C, after maturity, sells it to D. Could any of these parties collect the note from A? If so, which ones?

9. A sells a bill of goods to B for $1,000, for which B indorses to A C's note, payable at the First National Bank of Chicago. At maturity C is insolvent. What steps must A take to hold B?

10. Suppose that A draws a draft on B, in favor of C; but B has no funds in hand belonging to A. What steps must C take to charge A?

11. Suppose a note reads: "I, J. S. Lee, president of the E. & M. Ry. Co., promise to pay, etc.," and is signed J. S. Lee, Pres. E. & M. Ry. Co., whose note is it?

12. Write a negotiable promissory note for $250, at three months, and state the day of the month when the same will mature. Also a draft for same amount and time, and give the technical names of all the parties.

13. A makes his note to B's order, and before delivery C signs his name on the back. B indorses it over to D. What is C's liability to B? to D?

14. A forges the name of B as drawer of a draft payable to himself, at ten days' sight. The drawee accepts and the bill passes by indorsement to C, an innocent holder, for value, and before maturity. What are the rights if any, of each holder against the acceptor? What rights has the acceptor against B?

15. A note payable "to order" was indorsed by A to B, "without recourse." B indorses in full to C. The note proved to be a forgery, and the maker refused payment. Can C collect from B? If so what steps must he take? Can he collect from A? Why?

16. A gives his negotiable note to B for $475. B alters the amount so that it calls for $575, and indorses the paper in full to C for value, before maturity, C knowing nothing of the alteration. Can C collect the $475 from A? What is the liability of A? Are there any circumstances under which C could collect the $575? If so, what are they?

17. A gives B his note payable "to order," and B indorses it "Pay C only." C indorses the paper to D in payment of a personal debt. What are D's rights?

18. Give the facts of a case in which A, in his own name, would have the right to sue B, though they never had any dealings with each other, and B does nor even know of the existence of A.

19. A gives B his non-negotiable note, which B transfers to C by an indorsement in full. What is the liability of A to C?

20. On the 18th of August A gave B his check in payment of a debt. B presented the check at the bank on the 25th, but the bank had failed, closing its doors at the close of business hours on the 19th. On whom will the loss fall, and why?

21. In the above case, suppose that on the 19th B indorsed the check to C, who goes on the 20th to present it, but finds the doors closed, as did B. On whom will the loss fall?

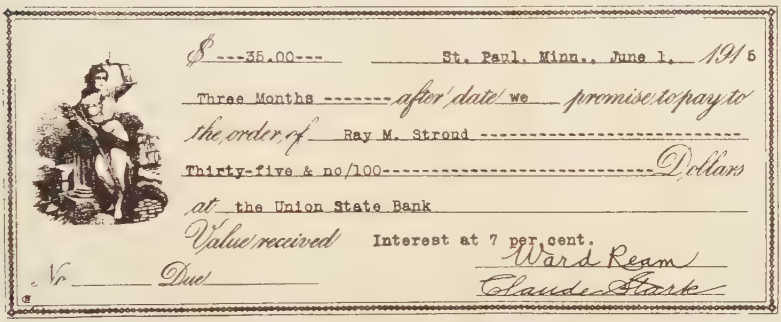
22. A drew his check in favor of B for $100. B indorsed it over to C, who raised it to $190. On presentation at the bank it was paid. Can the bank recover from C, and if so, how much? Are there any circumstances under which A or B would be liable?

23. A gave his note to B at 60 days. After the note was given B was adjudged a lunatic, and a conservator appointed for him. B, however, still retained the note and sold it to C for value. C indorsed it without recourse to D, who held it at maturity. What is C's liability?

24. A engaged B to make a large purchase of corn for him, and left with him for that purpose a blank promissory note signed. B did not make the purchase, but filled out the note for a large amount and indorsed it over to C for value before maturity, C knowing nothing of B's bad faith. C indorsed it for value to D, who knew of the origin of the paper. Can D collect it?

25. B sent his collector to A for a settlement of his account. A gave him his check payable to B or bearer, but on his return the collector lost the check. C found the check and sold it to D. Can B stop payment of the check by notifying the bank?

26. Inspect the following instruments:



$ ---35.00--- St. Paul, Minn., June 1, 1916

Three Months ------- after date we promise to pay to the order of Ray M. Stroud ----------

Thirty-five & no/100---------- Dollars

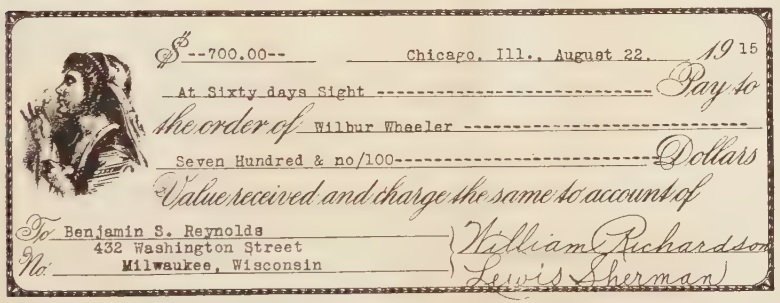
at the Union State Bank

Value received Interest at 7 per cent.

No. ____ Due ____

Ward Ream

Claude Stark



$ --700.00-- Chicago, Ill., August 22, 19 15

At Sixty days Sight ---------- Pay to the order of Wilbur Wheeler ----------

Seven Hundred & no/100---------- Dollars

Value received and charge the same to account of

To Benjamin S. Reynolds
432 Washington Street
Milwaukee, Wisconsin

No. ____

William Richardson

Lewis Sherman

In each of the above instruments, who are the parties primarily liable? Who secondarily liable? To whom should presentment for payment be made and where? To whom should notice of dishonor be sent, if the draft is not paid?

# CHAPTER XXI

## INTEREST

**222. Interest** is the use of money. For this use the user pays the owner a consideration, usually stated as a given per cent of the principal sum for each year of use. In popular language the money paid for interest in itself called the "interest," though this is not strictly correct.

**223. Simple Interest** is interest computed solely upon the principal sum, as distinguished from compound interest.

**224. Compound Interest** is interest computed upon the principal sum and also upon unpaid sums due for interest. Compound interest is of two kinds: (*a*) Simple interest upon unpaid interest due upon principal, often called *annual interest;* (*b*) interest upon interest upon interest *ad infinitum.*

The general rule is that in the absence of contract therefor, express or implied,* or of some statute requiring it,† compound interest is not allowed to be computed upon a debt. This rule includes both classes of compound interest.

Even when there is a contract therefor, the right to collect compound interest is denied in some states, unless such contract is independent of the principal contract and be *made after the simple interest is due.* Leonard vs. Villars, Admr., 23 Ill. 377; First National Bank of Galesburg vs. Davis, 108 Ill. 633; Harris vs. Bressler, 19 Ill. 467.

*Compound Interest ad infinitum* is legal only in California, Montana, Iowa, Tennessee, Missouri, Nebraska, and Texas. In Missouri interest may not be compounded oftener than once

* Compound interest has been implied in specific cases, because of a generally prevailing usage in a given line of business or because peculiar circumstances have required it, in California, Dakota, Iowa, Tennessee, Kentucky, Massachusetts, Michigan, New Hampshire, New Jersey, New York, and Vermont.

† Compound interest is usually allowed by statute in the calculation of refunds in case of misappropriation of trust funds by executors and administrators. In this case it is in the nature of a penalty.

a year. In Nebraska and Texas interest may be compounded up to the point where the total interest equals what it would be at the maximum legal rate, but not beyond that.

*Annual Interest.* The general rule is that if interest is not paid when by the terms of the original contract it falls due, it does not draw interest, but in most states, the parties have a right to contract in advance that if unpaid it may itself bear simple interest.*

Simple interest upon principal, in case of a note, is sometimes evidenced by coupon notes attached to the principal note, these coupon notes being themselves interest-bearing.

**225. Simple Interest Always Presumed.** The court will never assume that compound interest of either class is due. In the absence of a specification in the contract, simple interest is always presumed.

**226. When Interest is Payable.** The general rule is that interest becomes due and payable at the same time as the principal, and not before, except by contract. Therefore, a note running longer than one year and bearing interest should state that the interest is payable annually if such is the intention; otherwise it cannot be collected until the note is due.

Ill. National Bank vs. School Trustees, 211 Ill., 500; Motsinger vs. Miller, 59 Kans., 573; Tanner vs. Dundee Land Inv. Co., 12 Fed. 646.

**227. Legal Interest** is that rate of interest prescribed by the law of the state or country which will prevail when there is no special agreement as to rate of interest between the parties.

Most states have also adopted a maximum lawful rate, beyond which parties may not validly contract for the payment of interest. This is called the *maximum rate.*

**228. On What Interest is Allowed.** The law allows interest only on contracts, express or implied, for the payment of interest, or as damages for the wrongful detention of money. Interest is

* Annual interest will be allowed by contract but not by inference in all states except Connecticut, Delaware, Idaho, Maine, Massachusetts, New Jersey, Nebraska, and Utah. In Nebraska the total interest contracted for must not exceed the interest upon the original principal at the maximum legal rate.

created *expressly* when the parties to a contract agree as one of its terms that interest shall be paid, which is usually done by inserting a clause which reads, "bearing interest," "with interest," or some similar expression. Interest is payable by *implied contract* when the parties make no express agreement therefor, but from the circumstances of their dealings the law implies that they contracted in reference thereto. Such circumstances may exist by virtue of the customs or usages of the particular trade which the parties are considered to have had in mind as a part of their contract, or because of the nature of previous dealings between the parties.

The commercial importance of interest is confined largely to debts, either in the form of negotiable instruments or otherwise. As a general rule interest is allowed on all written instruments stipulating the payment of money, interest being allowed after the payment is due. In accordance with this rule, no interest is allowed on negotiable paper before maturity unless the words "with use," "with interest," or some equivalent expression be made a part of the note. The statutes of the various states provide for the allowance of interest upon judgments after they have been rendered, and the rate allowed is ordinarily that rate which is the legal rate in the state where the judgment is rendered.

**229. What Law Determines the Rate.** The rate of interest which a contract bears, and also the question whether it bears interest at all, are both determined by the law of the place where the contract is expressly or impliedly to be performed. If no place of performance is specified, it will bear interest according to the law of the place where it was made.

If a draft be drawn in Wisconsin for a debt payable there, upon a person in Illinois, and the draft be not accepted, an action may be brought by the holder against the drawer, and the laws of Wisconsin respecting interest will apply. On the other hand, if the draft had been accepted in Illinois and an action were brought against the acceptor, the laws of Illinois respecting interest would govern. All misunderstanding may be avoided by the parties expressly providing for a rate of interest, or providing that the laws of a particular state shall control.

**230. Interest on Accounts.** If goods are sold on terms of credit which make the bill payable on a certain day, and the bill is not paid on that day, interest is due thereafter, whether so

specified or not.* Many business houses specify this, however, so that there shall be no misunderstanding. If goods are sold on credit without any specified date of payment, interest cannot be collected unless there is a special agreement to that effect. If a balance be agreed upon as of a certain date, however, this will render it liquidated so as to draw interest thereafter. When there has been a demand for payment of a balance due, and this demand has been wrongfully refused, the demand has the effect of a liquidation of the account and interest is allowed from the date of the demand.

**231. Interest on Partial Payments.** When a debt is carrying interest, and a partial payment is made, a question arises as to whether this payment should be credited upon the interest then due or upon the principal debt. Three rules, known as the *United States rule*, the *Connecticut rule*, and the *Merchants' rule*, have been developed by the courts. The United States rule is the rule applied in practically all the states in the absence of a special agreement between the parties. This rule is as follows: "When a partial payment is made, apply the payment in the first place to discharge the interest then due. If the payment exceeds the interest, the surplus goes towards discharging the principal and the subsequent interest is to be computed on the balance of the principal remaining due. If the payment be less than the interest, the surplus of the interest must not be taken to increase the principal; but interest continues on the former principal until the period when the payments, taken together, exceed the interest due, and then the surplus is to be applied toward discharging the principal; and interest is to be computed thereafter on the balance."†

* The student must bear in mind that the forbearance of creditors — the fact that creditors do not as a rule insist upon this right — does not in the least affect the legal status of the right. Interest can be legally collected on overdue accounts, by any creditor, in any of the cases above enumerated.

† This statement of the rule was made by Chancellor Kent in the case of Connecticut vs. Jackson, 1 Johns Ch. (N. Y.) 13. It has been expressly approved in Delaware, Florida, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Missouri, Nebraska, New Hampshire, New Jersey, New York, North Carolina, Ohio, Tennessee, Texas, Utah, Virginia, Wisconsin, West Virginia and Kansas. It is not followed in Connecticut, as is noted in the text, but in all other states it may be safely predicted that the United States rule would be applied by the courts should the question be presented to them.

The *Connecticut rule* has application in Connecticut only. It is a modification of the United States rule to the extent that it provides that the first partial payment shall not be applied to the extinguishment of the interest, unless such payment be made at least one year from the time when the interest began to run, nor shall subsequent partial payments be so applied unless there is at least one year between them. This is upon the ground that interest cannot be due except from year to year.*

The *Merchants' rule* is also comparatively unimportant. The custom is prevalent in some mercantile centers in the settling of accounts to charge interest on all debit items and to allow interest on all credit items, interest on each item being figured from the date of the item until the date of the settlement or adjustment. This is known as the merchants' rule. It is only applied by the courts when there is an express or implied agreement between the parties to adopt this as the correct means of computing the interest. In a few instances proof of a course of dealings, or custom between the parties, has been recognized as sufficient to establish an implied contract to apply the merchant's rule. In general, however, it is stated that he who seeks to employ this rule has the burden of proving an agreement to adopt it. †

**232. Usury** is an illegal or exorbitant rate charged for interest. Any rate beyond the maximum rate allowed by law is usurious. The penalty for contracting for a greater rate varies in the different states, and a contract may be usurious in one and perfectly valid in another.

All kinds of subterfuges are resorted to in order to avoid the penalties provided for usury. Sometimes the borrower is required to receive a small article of personal property at an

* This rule was adopted by the Supreme Court in Connecticut at an early date, *i.e.*, 1784. Kirby's Reports, p. 49; Kissam vs. Burral, Kirby 335; Treat vs. Stanton, 14 Conn. 457. It continues to be the law in that jurisdiction.

† The following cases have recognized the merchants' rule as the correct method of computation of interest under special circumstances: Stoughton vs. Lynch, 2 Johns Ch. (N. Y.) 210; Smith vs. Shaw, 2 Wash. 167; Hart vs. Dewey, 2 Paige (N. Y.) 207; Backus vs. Minor, 3 Cal. 231; Pearson vs. Grice, 8 Fla. 214; Berkey vs. Gay (Mich. 1904) 100 N. W. 920. In the last named case this rule was confused by the court with the Connecticut rule. The right to imply an agreement to use the merchants' rule has been expressly denied in Averill vs. Verner, 22 Oh. St. 372, and Lewis vs. Bacon, 3 Hen. & M. (Va.) 89.

exorbitant figure, and in this manner the lender endeavors to get an extra return on his money over the legal rate. In all such cases the law looks to the intent, and if the contract appears to have been devised for the purpose* of securing a usurious rate the courts will impose the penalties. As a general rule, if an obligation has already been paid together with a usurious rate of interest, the penalty will not be applied, and the debtor cannot recover his money, though this rule is modified in some states.

When a note executed in one state is made payable in another, the law of the state of performance will govern in determining whether or not the instrument is usurious. 140 U. S. 101.

It is not deemed usurious for interest to be taken in advance, neither is it unlawful to purchase a third person's note at a great reduction from its face value, for in such cases the reduction is not intended as a means of escaping the penalty for an unlawful rate but represents the profits which the buyer demands as return for his assuming the risk of being able to collect the obligation. Similarly, if money is loaned at a risk, and the contract provides that interest is to be paid out of the profits or not at all, the collection of a high rate is not usury, for the lender is entitled to large returns in the event of the success of such an enterprise.

When a borrower pays a broker a fee for finding him a lender, this fee does not make the contract usurious. But if the money which the borrower receives really belongs to the broker, and the fee is not paid merely as a charge for his time and expenses in negotiating the loan, the contract may thereby become usurious, for otherwise the purpose of the statutes relating to lawful interest would be thwarted.

A table showing the legal rate, maximum lawful rate, and the penalties provided for usurious contracts in the several states is given in the appendix.

## REVIEW QUESTIONS

1. Ames gave Smith his note for $500 payable on demand. No provision was included as to the payment of interest. May Smith collect interest on this obligation? From what date? What rate? Why?

* The fact that the consideration is small will not of itself be considered evidence of usurious intent, for the law does not weigh consideration.

2. On July 1 Jones gave Brown his note at sixty days for $100, but no mention was made of any interest. If this note is paid at maturity what amount may Brown demand?

3. In the above case, the note was not paid until October 1 following. What amount may Brown claim in your state?

4. A, being pressed for funds, borrowed $500 from B and agreed to pay him two per cent a month for interest. If the note be for nine months, how much can B collect in your state at maturity?

5. A, of Denver, borrows of B, of Chicago, $1000, on a note for ninety days, payable at the First National Bank of Chicago. The note bears interest at twelve per cent per annum. Is this usury, and if so, how much can be collected?

6. On Oct. 26, 1916, Erskine gives two notes to Blair each for $3000 and due in three years. One reads "With interest at 6% per annum"; the other reads, "With interest at 6% per annum payable annually." If each of these notes is paid in full when due and no part is paid until due, what must be the amount of the check given to pay each of the notes on Oct. 28, 1919?

7. A, a minor, was indebted to B. He gave in payment his note, which B indorsed in full to C. Is A liable to C? Is B liable?

8. In the above case suppose B had indorsed without recourse. Would he then be liable?

9. A purchased from B a bill of goods to the amount of $200. A gave him, without indorsement, C's note payable to bearer for $200. (*a*) Suppose C is a minor; (*b*) suppose C's signature be forged; (*c*) suppose C prove to be insolvent; is A liable in any case?

10. A draft on B payable to C and purporting to be drawn by A was presented to B and he accepted it. B afterward learned that A's signature was forged and when the draft was presented for payment by D, an innocent indorsee, B refused to pay it. What are the rights of the different parties?

11. A note is payable to L. M. Swift and he wishes to transfer it to C. M. Miller without becoming responsible for its payment. Write his indorsement.

12. Suppose he wished to indorse it so it would not be further negotiable, how could he do it?

13. A note payable to order was stolen from the owner and his indorsement forged thereon. After passing through several subsequent holders' hands, the owner discovered the note in a bank. What are his rights as against the bank—can he secure the possession of the note and if so what is the name of the action he must bring?

14. A, when indorsing a negotiable promissory note wrote over his signature the words "presentment, demand, protest, notice, and waived." At maturity the note was not paid, in fact was not even presented. Is A liable? Why?

15. A gives his note to B payable at Union National Bank. B presents the note there at maturity. Is the bank authorized to pay it and deduct the amount from A's account?

## CHAPTER XXII

## GUARANTY AND SURETYSHIP

**233. Definitions.** A *surety* is one who makes an unconditional promise, in writing, to be responsible for the debt of another. A *guarantor* is one who agrees, in writing, that under certain conditions he may be held responsible for the payment of some debt or the performance of some duty by another. The contract of a surety is called a *contract of suretyship*; the contract of a guarantor is called a *guaranty*.

**Degrees of Liability.** There are in general four degrees of liability assumed by those who become liable with or for others. Named in the order of onerous liability they are:

1. Co-Maker.
2. Surety.
3. Guarantor { *a.* For Payment. *b.* For Collection.
4. Indorser.

**234. In Writing.** Contracts of guaranty or suretyship, being contracts to answer for the debt, default, or miscarriage of another, come under the Statute of Frauds and must be in writing. The writing may be on the original instrument of debt or obligation, or may be on a separate paper.

**235. Consideration.** If a contract of guaranty or suretyship be made at the same time as the original contract which it supports, the making of the original contract is considered sufficient consideration to support the contract of guaranty or suretyship. This is because the performance of an act which one would not otherwise perform, is a consideration, and the making of the original contract is such an act. There need be no other consideration.

But when the contract of guaranty or suretyship is made subsequent to the original contract which it seeks to support, there must be a separate consideration, since a past consideration will not support a new contract. This new consideration may be

something given to the guarantor, for instance, a payment of money; or the relinquishment of a right by the creditor, for instance, the surrender of securities in his hands. Some states* require that the consideration be stated in the contract of guaranty or suretyship.

EXAMPLE

Solway owes Jenkins $500. Kasson writes to Jenkins as follows: "I will pay what Solway owes you, if he does not, (Signed) Kasson." This is a guaranty of past credits and unless some consideration passes between Jenkins and Kasson the agreement cannot be enforced. If, however, Kasson writes "If you will extend Solway's credit for ninety days, I will pay you what he now owes you, if he does not, (Signed) Kasson," and this offer is accepted by Jenkins, there is a sufficient consideration to support the promise of the guarantor.

**236. The Contract of Surety.** The surety usually signs the original instrument with the promisor for whom he becomes liable. He should write the word *surety* after his name, to indicate the nature of his liability. If he fails to do this, he is a co-maker, except as to those who are cognizant of the suretyship.

**237. Liability of a Surety.** It is the duty of the surety to seek out the creditor at maturity and see that the debt is paid. Surety and principal are jointly and severally liable to the creditor.

The surety is therefore liable as soon as default is made, and no demand upon the principal debtor or notice of his default is necessary. This liability on the part of a surety is a continuing liability. Delay on the part of the creditor to enforce collection from the debtor will not release the surety.

EXAMPLE

Ames talks with his banker about the loan of $1000. The bank agrees to lend him the money if he will secure the joint note of himself and Bates. They sign such a note and the bank advances the money. Upon non-payment, the bank may sue both Ames and Bates jointly, or may sue Bates alone.

**238. The Contract of Guaranty.** A guarantor either signs a paper separate from that signed by his principal, or signs the same paper in such a way as to indicate clearly that his contract is not one of primary liability.

*A statement of the consideration is required in Alabama, Georgia, Minnesota, and New York to validate a contract of suretyship or guaranty.

EXAMPLE

Caldwell desires to secure credit from the Hub Clothing Company for a suit of clothes. He takes with him a letter from Murphy to that company in which Murphy agrees that if the company will give Caldwell credit up to $75 he will pay it if Caldwell does not. If in reliance upon this letter the Hub Clothing Company extends credit to Caldwell, Murphy becomes liable as a guarantor.

**239. Guarantor's Liability.** A guarantor's liability is less stringent than that of a surety, or to speak more exactly, he has an opportunity of avoidance that is denied to the surety. The guarantor has a right to expect that demand for payment will be made upon the principal within a reasonable time after maturity, and that notice will then be given to him (the guarantor) in case of default. If this be not done, the guarantor is *discharged to the extent that he was damaged by the delay.*

In this respect the contract of guaranty is more onerous than that of indorsement, for failure of due presentment and notice discharges an indorser *absolutely*, whether or not he has suffered by the delay.

It is not always easy to determine whether a sponsor is a surety or a guarantor. This is more often determined from the nature of the agreement than from any express wording or form used. If the nature of the agreement is such that sponsor and principal are jointly and severally liable, the sponsor is a surety. If the liability of the sponsor is secondary to that of his principal, the sponsor is a guarantor.

Contracts to answer for the performance of the duties of others are always guaranties, not contracts of suretyship. Fidelity bonds are contracts of this kind.

**240. Classification of Guaranties.** Guaranties are variously divided, the following being the most common and important classes:

Classes of Guaranties
- As to Operation
  - *a.* General
  - *b.* Special
- As to Subject-matter
  - *a.* For Payment
  - *b.* For Collection
- As to Amount
  - *a.* Limited
  - *b.* Unlimited
- As to Time
  - *a.* Temporary
  - *b.* Continuing

A *special* guaranty is one directed to a particular person.

A *general* guaranty is directed to whomsoever may accept the offer made. Being in the nature of a proposition, it must be accepted before it is binding, and the guarantee must notify the guarantor. This is necessary that he may know to whom he is liable, and for what amount, that he may take proper steps to protect himself against loss.

In case of any guaranty it is safer to notify the guarantor of its acceptance.

General Guaranty

*Temple, Tex., Sept.* 1, 1916.

*To any one who shall accept and retain this letter of guaranty, I will guarantee the payment of any bill of goods which may be sold the bearer, G. W. Brown, to an amount not exceeding four hundred dollars. This should be considered for one transaction only.* *N. Y. BLAIR.*

Special and Limited Guaranty

*Ross Grove, Ill., Aug.* 16, 1916.

*A. C. McClurg & Co., Chicago, Ill.*

*Gentlemen: If you will sell the bearer, James Allen, a bill of goods on ninety days' credit, I will cheerfully guarantee the payment thereof to an amount not exceeding one thousand dollars.* *JOSEPH B. LYONS.*

**Guaranty for Payment.** A holder of a negotiable paper writes on the back thereof:

*For value received I hereby guarantee the payment of the within note.*

*A.*

This is an absolute guaranty, for the guarantor is liable immediately on the default of the debtor. But he is entitled, according to the weight of authority, to demand and notice within a reasonable time.

**Guaranty for Collection.** If the guaranty be as follows:

*For value received I hereby guarantee the collection of the within note.* *A.*

or

*For value received I warrant this note good.* *A.*

it is a guaranty for collection. The sponsor does not absolutely guarantee that the note will be paid at once without diligent effort to collect, including suit if necessary or worth while, but that the debtor can be made to pay it.

*As to Amount.* A guaranty may be for a certain amount, in which case it is said to be limited, or it may be for an unlimited amount.

*As to Time.* A guaranty may be either temporary, that is, limited to a single transaction, or continuing. A continuing guaranty applies to successive transactions. It is often extremely difficult to determine whether the contract be a temporary or continuing one, and therefore it is best to have the instrument itself state plainly which is intended. If it contains such expressions as "from time to time," or "at any time," or "for any debt," etc., it is usually construed as a continuing guaranty. A continuing guaranty will not only cover bills up to the amount of the guaranty, but if they are paid and others bought it will cover any balance due within the limit named until extinguished.

CONTINUING GUARANTY

*Chicago, Ill., July* 18, 1916.

*J. W. Butler Paper Co., City.*

*Gentlemen: For all goods that you may sell E. P. Farr, upon the usual terms of credit, I will for value received, guarantee the payment in an amount not exceeding one thousand dollars. You are at liberty to consider this letter a Continuing Guaranty until further notice.* *H. TEMPLETON.*

**241. Rights of Surety.** Up to the time when the surety has been compelled to pay, he has the right to bring suit in a court of equity to compel the debtor to pay. In the absence of statutory provisions permitting it, however, he cannot bring such a suit in a court of law.

After the surety has paid the obligation for which he became surety, he has three separate rights:

(1) The right of indemnity against the principal debtor.

(2) The right of contribution from co-sureties.

(3) The right of subrogation, against the former creditor.

It is the possession of these rights that makes the liability of the surety less onerous than that of the co-maker.

*Indemnity.* This is the right of the surety who has paid his principal's debt to sue the principal in his own name for the amount paid, plus interest and costs.

*Contribution.* If there are two or more co-sureties, and one pays the debt for which both or all became surety, the one paying

the debt has the right to compel each of the others to pay him such an amount that the burden of the loss will be distributed equally among the co-sureties. This is called the right of contribution.

EXAMPLE

A, B, and C jointly become surety for D. When the debt is due D fails to pay it, and the creditor demands payment of C, who pays it. C now has the right of contribution against A and B to compel them each to pay one-third.

*Subrogation.* When a surety pays the creditor, the obligation is not discharged as to the debtor. The latter is just as much in debt as ever, but to a different person. The surety now stands in the place of the erstwhile creditor. He has a right to insist on all the securities which the creditor had, for the payment of the debt. If the creditor has secured a judgment against the debtor, the surety is now entitled to the benefits of it. This is called the right of subrogation.

**Rights of Guarantor.** The four rights enumerated above, for the surety, also belong to the guarantor under the same conditions.

**242. Discharge of Surety.** Of course a surety is discharged from further liability by paying the obligation for which he became surety, but there are a number of conditions under which he may be discharged without payment. The most important are:

I. Fraud practiced on the surety.
II. Diversion from the agreed purpose.
III. Alteration.
IV. Release.
V. Extending time to principal.
VI. Parting with security.

**Fraud Practiced on the Surety.** When one is induced to become a surety, or, for that matter, a drawer or endorser, for another, and there is a misrepresentation or concealment of a material fact, which if known to him would have prevented his entering upon the contract, it is void as to all parties having knowledge of the fraud.

EXAMPLE

A, securing a position of trust with a corporation, induced B to go on his bond for the faithful performance of his duties for one year. During the year A was found to have embezzled, but nothing was done about it, and the company, relying on his promise to make it good, took his note. The next year B, in ignorance of A's former misdeeds, again became his surety. In a short time A was again an embezzler, when the company notified B of their intention to hold him responsible on his bond. B was not liable, for he had been imposed on. The concealment practiced by the corporation was a fraud on the surety.

**Diversion.** When a bill is drawn or accepted, or a note made or endorsed for accommodation, with an agreement that it is to be used for a particular purpose, any diversion in its use discharges the accommodation party as to all who have notice of the diversion. Any one taking such a paper with a knowledge of its diversion, is not a *bona fide* holder.

**Alteration.** Any alteration in the original contract which will release the principal will also release the surety. Any alteration in the contract of guaranty which would make any other contract void will make void the contract of guaranty.

**Extending Time to Principal.** The creditor should preserve his right against the debtor intact, not for himself alone, but for the benefit of the surety as well. When he relaxes his hold upon the debtor, he impairs the hold the surety would have when substituted (subrogated) in his place, and such an act releases the surety.

If the creditor makes a new contract with the debtor, extending his time, the surety is released. It does not follow, however, that mere forbearance to sue releases the surety, for if the *right to sue* has not been relinquished by a binding contract, the surety is not deprived of any of his rights. If the creditor wishes to extend the debtor's time, he should first obtain the surety's assent.

EXAMPLES

1. Callahan has guaranteed that Bell will pay a bill owing to Jordan which is due in thirty days. Jordan, without securing Callahan's consent, and for a consideration, extends the time of payment to ninety days. This releases Callahan.

2. Morgan is the guarantor of an obligation owing from Green to Lumley. The obligation becomes due and Lumley delays bringing suit against Green for three months. This does not discharge Morgan.

**Parting with Securities.** Upon the payment of the debt, the surety is entitled to all the rights, remedies, and securities which the creditor could have enforced. The creditor must, therefore, use every care that he do nothing to impair the surety's rights. He must not part with any securities he may have belonging to the debtor, and if he does so, the surety is released to the extent that he is damaged thereby. This has been held true even when the surety did not know of the existence of the security at the time of its release.

**243. Discharge of Guarantor.** A guarantor is discharged by any act of the creditor that would discharge a surety. All that has been said in this connection in regard to sureties applies equally to guarantors. In addition, however, a guarantor may be discharged by failure to make demand, or by lack of notice. It would perhaps be speaking more accurately to say that his liability in this case had never been perfected.

**244. Miscellaneous Matters—Indorsers and drawers and guarantors may become sureties.** Those who make themselves liable for the debts, defaults, or miscarriages of others become fully liable as soon as conditions precedent to their liability fasten this liability upon them. The distinction between them, then, is not one of *degree* of liability; but of greater or less opportunity for the avoidance of the liability. The indorser is discharged absolutely if presentment is not properly made and notice promptly given, but if these things are properly attended to, his responsibility at once becomes as great as that of the surety. Similarly, the guarantor has a loophole for the avoidance of liability that is denied the surety, but if the creditor properly attends to those matters necessary to fix liability upon the guarantor, including an unsuccessful attempt to collect, then the liability of the guarantor is as great as that of the surety.

**Death of a Joint Guarantor.** By the common law, the death of a joint guarantor releases his estate from obligation as guarantor. This rule has been changed by statute in some States.

**Guaranty Not Negotiable.** In many States guaranties are held to be non-negotiable. It would seem prudent, therefore, to rely but little on an assigned guaranty.

EXAMPLE

B held A's note, which he sold to C, writing under his blank endorsement the words, "I guarantee the payment of this note. B." A subsequent holder of the note sued B on this guaranty, but the court held that the guaranty was personal to C.

The guarantor can always make sure that his guaranty is personal to the one to whom given by adding to it the words, "This guaranty is non-assignable."

**Guaranty Valid Though Principal Debt Not Enforceable.** Sometimes a guaranty or surety is requested because the principal debt is not enforceable, as when a minor asks for credit, which is granted if security be given. In such cases the guarantor or surety is liable even though the principal debtor is not.

**Promises to Pay One's Own Debt.** A guaranty to pay one's own debt need not be in writing. If A induces B to give an accommodation note for A's debt to C, A's guaranty of the note is valid even though verbal.

If A orders goods to be delivered to B, saying to the merchant, "Charge them to me," or "I will pay for them," it is A's own debt and the promise to pay need not be in writing. If he says, "If B does not pay, I will," it is a guaranty and is not valid unless in writing.

**Failure to Receive Notice of Acceptance or Default.** While the better course is for a creditor to give immediate notice of the acceptance of an offer of guaranty, many states adopt the view that there is a sufficient acceptance if the creditor advances money or goods to the principal debtor in reliance upon the contract of guaranty. In more than half of the states, however, the rule followed is the so-called Massachusetts rule, which declares that the guarantor is not bound until he has had notice of the extension of credit.

**Revocation by Surety or Guarantor.** A notice of revocation of the agreement of guaranty is effective if it is given to the creditor before he has made advances in reliance upon it. But if he has already acted upon the offer the guarantor cannot escape liability by revoking the contract. After notice of revocation of a continuing guaranty has been received the creditor can hold the guarantor only as to past advances.

## PRACTICAL SUGGESTIONS

**If You Are a Surety or Guarantor.** Protect yourself by limiting the agreement of suretyship as much as possible. Require notice of acceptance and default within a reasonable time, and limit your liability to a maximum amount. Otherwise, you will assume a much greater liability than you would as a partner.

Never sign an agreement of suretyship without carefully investigating the person whom you are guaranteeing. Make a specific request for information from the creditor. Never become surety for a man with whom you would hesitate to enter into a partnership agreement.

**If You Are a Creditor Relying on an Agreement of Suretyship or Guaranty.** Require that the agreement be in writing and signed by the surety. Also require that it state the consideration. Be careful to conform to all the requirements of the agreement, and to protect yourself against all possible question give notice within a reasonable time of acceptance and of any default of the principal. Disclose all material facts to the surety regarding the principal. Do not alter the agreement, or vary its terms, or surrender any securities in your hands to the principal, without the consent of the surety.

The court will never enlarge the liability of the guarantor or surety, by construction. Contracts of guaranty and suretyship are always construed strictly according to their wording.

## REVIEW QUESTIONS

1. A went into B's clothing store with C and said to B, "You fit C out with a suit of clothes and I will pay for them." B furnished C a suit and sent the bill to A, who ignored it. B thereupon sued A, who defended the action on the ground that his promise was not in writing. May B recover against A? Why?

2. Jones owes Smith $100, Brown owing Jones a similar amount. Brown promises to pay Smith $100 for Jones if Jones will release him (Brown) from his debt of $100, and this is agreed to by Jones. What, if any, defense would Brown have to a suit by Smith against him for $100?

3. Steele and Newson both signed a promissory note, on which money was to be loaned by Wood to Newson, Steele signing as a surety. Newson later, with the knowledge of Wood, altered the date from September 11 to October 11 and delivered it to Wood. It being unpaid, Wood sued Steele, who claimed that these acts had served to discharge him. May Wood recover against Steele? Why?

4. Jones, an employe of Railton, requested Matthews to execute a bond for the performance of his duties as Railton's cashier. Matthews made inquiries regarding Jones, and was informed by Railton that Jones was considered a reliable man. As a matter of fact Jones had ten years previously

embezzled $560 of his employer's money, but had repaid the amount and had been guilty of no misconduct since that time. Railton failed to inform Matthews of any of these facts. Matthews executed a surety bond to Railton for Jones' fidelity. Two months later Jones absconded with $10,000 and Railton sued Matthews on the bond. May he recover? Why?

5. Ames, a surety on a note that was due and unpaid, was sued. His defense was that the maker of a note was an infant. Was Ames liable?

6. The Fidelity Bond Company gave a cash bond of $10,000 to the State of Wyoming for the faithful performance of contract by the National Bridge Co. The bridge contracted for collapsed a week before the date when it was to have been completed. Two weeks later the officers of the National Bridge Co. left the country for parts unknown, after realizing all they could from the assets of the company. The State then notified the Fidelity Bond Company that its bond was forfeited. What rights had the bond company? Why?

# CHAPTER XXIII

## SALES OF PERSONAL PROPERTY

### The Contract of Sale

- I. Essentials
  - 1. Competent parties
  - 2. Mutual assent
  - 3. Consideration
  - 4. Legal subject matter
  - 5. Conformity to Statute of Frauds
- II. Transfer of Title
  - 1. Between buyer and seller
    - a. Ascertained goods
    - b. Unascertained goods
  - 2. As to third parties
    - a. Subsequent purchasers
    - b. Creditors
  - 3. By conditional sale
  - 4. By chattel mortgage
  - 5. By documents of title
    - a. Straight receipts
    - b. Negotiable receipts
- III. Warranties
  - 1. Express
  - 2. Implied
    - a. Title
    - b. Quality
- IV. Remedies
  - 1. Of seller
    - a. Primary
      - a. Collection
      - b. Damages
    - b. Secondary
      - a. Lien
      - b. Stoppage in transit
      - c. Resale
      - d. Rescission
  - 2. Of buyer
    - a. For breach of contract
    - b. For breach of warranty

**245. Introduction.** The ownership of personal property would be of little value to the business man unless he also had the right to transfer it to others. The transfer of property in goods forms the basis of the majority of the transactions of commerce. The law applicable to such transfer is called the Law of Sales of Personal Property, or of Goods.

There are three phases of the Law of Sales which must be understood by a business man who seeks to transfer his property in goods to another intelligently. These are:

1. Manner and time of effecting a transfer of title to personal property from buyer to seller.

2. The express and implied warranties incident to a contract of sale.

3. The respective remedies of the buyer and seller.

These three points, *viz.*, transfer of title, warranties, and remedies, are separately discussed in Chapters XXIV-XXVII.

**Sales and Contracts to Sell.** A contract to sell is one in which the seller agrees to transfer the property in goods to the buyer at some other time for a consideration called the price. When the seller has transferred the property in the goods to the buyer, the transaction is called a *sale*. Prior to the transfer it is merely a *contract to sell*.

EXAMPLES

1. A, a coal dealer, says to B, "I will sell you your next year's coal supply for $8 a ton, if you will agree to buy fifteen tons." B says, "I accept that offer." This is a contract to sell. B acquires the right to demand the transfer of fifteen tons of coal at a future date. Meanwhile A bears the risk of loss and the coal is subject to levy and execution for his debts.

2. C goes to D's grocery store, asks for a bag of flour, receives it and pays the price. This is a sale, because the property in the goods is transferred. If D should become a bankrupt his creditors could not reclaim the bag of flour from C.

**246. Essential Elements of Contract to Sell.** A contract to sell goods must possess every element essential to the validity of a simple contract. It must be made between competent parties, must by its terms evidence a mutual assent, must be made for a valuable consideration, and must concern a legal subject matter. Furthermore, it must comply with the Statute of Frauds.

In a contract to sell goods the parties are the seller and the buyer; the consideration is the price which the buyer agrees to pay; and the transfer of the ownership in the goods which the seller agrees to sell forms the subject matter of the sale.

**247. Who May Sell.** Only the true owner of goods or his legal agent may sell them so as to transfer a valid title to the buyer. Herein is the difference between the transfer of title to negotiable instruments and the transfer of title to other articles of personal property. While the thief or finder of a negotiable instrument which is payable, on its face or by indorsement, to bearer, or the thief or finder of money, may transfer it to a holder in due course so as to give him a title valid against the whole world, and even against the person from whom it has been stolen or who has lost it, the thief or finder of other personal property can transfer no title, because he has none himself. The true owner may reclaim it even from an innocent purchaser who has paid value. A person, therefore, however innocent, who buys goods from one not the owner, obtains no property in them as against the true owner; nor does anyone to whom he ever sells them obtain good title as against the true owner.

EXAMPLE

Soltau sued Gerdau to recover a quantity of rubber. In the trial of the case it was shown that Gerdau had bought the rubber from Smith, a broker in Boston, who had acquired it from Soltau under circumstances which the court held amounted to theft. Therefore Soltau, as the true owner, was allowed to recover the rubber from Gerdau. Soltau vs. Gerdau, 119 N.Y. 380.

**248. The Thing Sold.** Strictly speaking, a person cannot sell goods which he does not own. He may *contract* to sell them, but he cannot *sell* them.

When one contracts to sell that which he does not own at the time, the contract is for the sale of "future goods." Any attempt to sell such "future goods" has the effect only of a contract to sell, and has not the effect of a present sale. Even if the seller in such a case should attempt to make the sale as a present owner, such an attempt has no effect, as the title remains with the true owner. It does have the effect, however, of making the supposed seller liable to the supposed buyer as on an executory contract, giving the buyer the right to exact performance or collect damages.

As a general rule, one cannot own that which is not in existence, and, therefore, things not in existence cannot be the subject of a present sale. An exception to this general rule is made in the case of growing products. Things which are the natural product or expected increase of things in existence have a *potential existence*, and if they are the product of things already belonging to the seller, they may be the subject of a present sale. This exception is recognized in most of the United States, as applied to the future crops from the seller's land, the future offspring of or products from the seller's animals, or wages to be earned under an existing contract. The only goods which are deemed to have a potential existence are growing crops and the unborn off-spring of animals. The Uniform Sales Act,* however, does not recognize the distinction and declares that all sales of future goods are merely contracts to sell and not sales.

In most States this exception will not be applied to crops not planted, or until the potential existence is actually begun in nature.

EXAMPLES

1. Fletcher contracts in April that he will sell to Murphy in September twenty bushels of tomatoes which he expects to grow on his vines. This is a contract to sell only, and Murphy possesses no property rights in any tomatoes until the contract is performed, and twenty bushels of tomatoes actually delivered.

2. Fletcher in July makes a present sale of thirty bushels of his growing tomatoes to Hatton, although the tomatoes are not yet ripe and both parties understand that the tomatoes are to be ripened on the vines. The property in the tomatoes is transferred to Hatton at once. His creditors may seize the tomatoes by an execution and levy. Fletcher has no title in them, and should he attempt to sell them to Jones, Hatton can reclaim them from Jones.

**249. The Price.** It is not necessary that the price be in money. It may be in other forms of personal property, and the character of the transaction will remain unchanged.

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* The Uniform Sales Act is a compilation of the laws regarding Sales of Goods, similar to the Negotiable Instruments Act, which has been recommended to the various states for adoption. It has not been generally adopted as yet, being in force only in Arizona, New Jersey, Connecticut, Massachusetts, Rhode Island, Ohio, and Wisconsin. The change in regard to the former doctrine of potential existence is one of the few changes in the existing law made by the uniform act.

EXAMPLE

Marcy agrees to sell Hines an automobile for 1000 bushels of potatoes or twenty tons of brick, as Hines may prefer. This is a contract for the sale of goods. If, however, the agreement had been to sell the automobile for an acre of land, the agreement would be governed by the laws relating to sales of real estate.

It is also unnecessary that the price should be specified, whether it be in money or in other personal property. The amount may be left for future determination, provided a way of determining it is agreed upon or understood, or may be determined by the previous course of dealings between the parties, or, if neither of these alternatives applies, the buyer must pay the reasonable value of the goods.

McConnell sold to Hughes 850 bushels of wheat at an agreed price of ten cents per bushel less than the Milwaukee price at any day thereafter which McConnell might select. McConnell delivered the wheat and notified Hughes that he selected March 24 as the day for determining the price. The Milwaukee market on that day was seventy-two cents a bushel, and this determined the price. McConnell vs. Hughes, 29 Wis. 537.

It is also possible for the buyer and seller to agree that the price shall be fixed at a future date by a third person. This is called a *sale at a valuation*. If the transaction be merely a contract to sell and the property in the goods has not been transferred, death or other circumstances making it impossible for the third person to fix the price avoids the contract. On the other hand, if the transaction be a sale and the buyer has received the goods, he must pay the reasonable value as the price, should the third person fail to specify it. If the third person is prevented from naming a price by the fault of either the buyer or seller, special remedies are provided. (See Chapter XXVIII.)

EXAMPLE

Johnson sells a horse to Brewer, the price to be fixed by Gordon after an examination of the horse. Before fixing the price, Gordon dies. If the horse has been delivered, Johnson may claim its reasonable value from Brewer; if the horse has not been delivered the transaction is terminated without the fault of either party, because of impossibility of performance.

If Gordon had fraudulently named an excessive price, or had been wrongfully influenced in naming the price by either of the parties, to the damage of the other, appeal could be made to the courts, which would then determine the reasonable value. Wendt vs. Vogel, 87 Wis. 462.

## REVIEW QUESTIONS

1. Evans, a farmer, sells to Barker, in the spring, the hay and corn that Evans will raise on his farm during the coming season. The corn has not yet been planted. He also sells to Barker the wool from 100 sheep, which he agrees to buy within thirty days, but which he does not yet own. In November, while he has the hay, corn, and wool in his possession, Evans' barn is destroyed by fire. Who suffers the loss as to each commodity? Why?

2. Hagins contracted to sell groceries to Combs and to take in exchange logs, and allow for the logs the most that the "seller could get offered in money for them, delivered at Oshkosh, when measured." Hagins delivered the groceries, and when Combs sought to pay him in logs, a dispute arose as to the number of logs which would satisfy Hagins' claim. What is the proper rule for determining the number? Is this a contract to sell goods? What goods?

3. Rodliff shipped some wool to Clementson, a wool broker, relying on his statement that he had a customer who would take the wool at once and pay cash, which he would remit to Rodliff. Instead of this, Clementson turned the wool over to Dallinger in payment of a debt which he owed Dallinger. What rights, if any, did Rodliff have against Dallinger? against Clementson? Why?

4. Corbett sold ten cords of wood to Moody, the wood to be inspected and valued by Jenner. After the wood had been delivered Moody paid Jenner $10 to place a low valuation on the wood, which he accordingly did, valuing it at $3 a cord. What rights, if any, has Corbett? How much may he recover for the wood?

5. Suppose that in the above example Jenner had departed for Europe before valuing the wood and remained away for ten years. What would the rights of the parties be (1) if the wood has been delivered; (2) if the wood had not been delivered?

## CHAPTER XXIV

## FORM OF CONTRACT OF SALE

**250. Statute of Frauds.** This statute was designed to make fraud difficult in important contracts. One of its provisions is that if a transaction involves a sale of goods of considerable value it is not enforceable unless evidenced by writing, or unless it shall have been partly performed, either by the delivery of some of the goods or the payment of a part of the price.

Some states in the United States have changed the limit of value in adopting this provision; others have not adopted it in any form. In the latter states it is not necessary that any contracts for the sale of goods be in writing to make them enforceable. The rules regarding the various states are listed in the foot-note to Section 118.

Some explanation of the terms of the provision is required.

**251. Goods, Wares, and Merchandise.** The requirements of this provision apply only to contracts for sale of goods, wares, and merchandise. They do not apply to contracts for the sale of work, labor, and materials. The contract of a shop-keeper to sell ordinary articles of commerce, such as potatoes, clothes-line, or needles, is a contract to sell goods, and if the value of the goods be more than fifty dollars (or whatever limit the particular state may have adopted) it must, if executory, be in writing or it will not be enforced. The contract of a noted sculptor, however, to make a statue of a particular person, is not a contract for the sale of goods, wares, and merchandise, but is a contract for work, labor, and materials, and will be enforced regardless of its form. Whether the contract belongs to the first or second class depends on the nature of the thing to be furnished. A contract for the sale of existing articles, or such articles as the seller manufactures in the ordinary course of his business for the general market, whether on hand at the time or not, is a contract for the sale of goods, wares, and merchandise, and the statute applies. On the other hand, if the goods are to be manufactured especially for

the particular buyer and upon his special order, not for the general market, the contract is for work, labor, and materials and need not be in waiting.

EXAMPLES

1. Garbutt, a miller, entered into a contract with Watson to sell him 100 sacks of flour to be ground from grain. No part was then delivered, no payment made, and no writing executed. When the flour was ground Watson refused to receive it, claiming that the contract was not enforceable because the price was more than $50. This was justifiable, because Garbutt ground the flour in the ordinary course of his business for the general market, and the contract was for the sale of goods, wares, and merchandise. Garbutt vs. Watson, 5 B. & A. (Eng.) 613.

2. Clay entered into an agreement to print a book for Yates, for which Yates had written the preface. When the book was completed Yates refused to receive it on the ground that the price was in excess of fifty dollars and the contract did not conform to the provisions of the Statute of Frauds. This was not justifiable, because this particular book was not suitable for the general market, and the contract was for the sale of work, labor, and materials, so that the Statute of Frauds did not apply. Clay vs. Yates, 1 H. & N; (Eng.) 73.

**252. Growing Crops and Standing Timber.** Timber is real estate until it has been cut. A contract to sell growing timber is not a contract for the sale of goods, but a contract for the sale of real estate. To such the Seventeenth Section of the Statute of Frauds does not apply, but contracts for the sale of standing timber must nevertheless be in writing, regardless of value, because the Fourth Section of the English Statute of Frauds, everywhere adopted in the United States, requires all contracts for the sale of land, or any interest in land, to be in writing. The result is that if there be a sale of uncut standing timber the contract will not be enforceable unless in writing; but if the timber has been cut, the agreement need be in writing only if the price is in excess of the statutory value, and if no timber has been delivered or part payment received, because cut timber is personal property.

On the other hand, whether growing crops are personal property or real estate depends upon the nature of the crops, and not upon whether they have been cut. Crops which are dependent for their growth upon cultivation by the hand of man may be sold before they are harvested, or severed from the soil, as personal property. They are goods, wares, and merchandise, and contracts for their sale need not be written if the value is less

than the statutory amount. But if the crops grow naturally without cultivation by man, they are treated as real estate until actually severed from the soil, and sales of them must conform to the provisions regarding sales of interests in land.

EXAMPLES

1. Armstrong entered into a verbal contract with Green to sell to Green the trees growing on his land, giving Green the right to cut and remove them within twenty years. Green cut a part of the trees, paying for the ones removed, but Armstrong refused to allow him to remove the remainder, claiming the contract to be unenforceable because it was for a sale of an interest in land and was not in writing. Green claimed that the contract was for the sale of goods, wares, and merchandise, and that although more than $50 in value, he had received and accepted part of the goods. The contract was for the sale of an interest in land and not enforceable. Green vs. Armstrong, 1 Denio (N. Y.) 552.

2. Parker sold a crop of potatoes to Staniland, the potatoes being in the ground on Parker's land, and Staniland agreed to dig them and pay a price per bushel. After digging a part of the potatoes and paying for them, Staniland refused to take the rest or pay for them, and when Parker sued him he claimed that the contract was not enforceable because not written as required of contracts for the sale of an interest in land. He was compelled to pay for the potatoes in the ground, the contract being for the sale of goods, of which he had accepted and received a part. Parker vs. Staniland, 11 East. (Eng.) 362.

**253. Determination of Value.** In determining whether the value in a given case exceeds the amount specified in the statute of frauds (fifty dollars in the English statute), the question properly is, what is the total value of all the goods bargained for in one sale or contract to sell? The mere fact that several different articles are bought, and that a different price is agreed upon for each article, does not necessarily prove that several contracts existed. If, however, from the intention of the parties it does appear that there were several distinct contracts, it is incorrect to add the various amounts together in determining whether the statute applies. This depends on the circumstances of the purchase and the intention of the parties.

EXAMPLES

1. Parker went to the shop of Baldey, a linen draper, and bought several articles of wearing apparel, none of which was of the value of fifty dollars, but which altogether were valued at $350. When the goods were delivered at Parker's home he refused to receive them, saying that he had changed his mind. Baldey was without remedy because the contract was verbal, no part received and accepted, no payment made and the value of the goods so sold in a single

sale amounted to more than the statutory limit. Baldey vs. Parker, 2 B. & C. (Eng.) 37.

2. Sheehan, who owned twenty shares of stock in the Colorado Springs Company, entered into a verbal agreement with Tompkins to sell the twenty shares which he owned, and also to sell as agent the shares of Smith, Jenkins, and Simmons. The value of the shares of neither Sheehan, Smith, Jenkins, or Simmons amounted to fifty dollars, but together the value was in excess of this amount. The agreement was valid and enforceable because each contract was deemed a separate contract, Tompkins having agreed to buy goods owned by different persons. Tompkins vs. Sheehan, 158 N. Y. 617.

**254. Not Enforceable by Action.** Contracts for the sale of goods are not enforceable by action unless they correspond with the provisions of the Statute of Frauds. This does not mean that the contracts are void, for the parties may perform them if they wish, but it does mean that neither of the immediate parties to the contract can enforce it against the other in court, should the other object. That the contract does not conform to the requirements of the Statute of Frauds is therefore a personal defense of the parties to the contract and is not an available defense to third parties, that is, third parties cannot escape liability on the ground that a contract between others did not conform to the requirements of the statute. Such questions may arise when a third party by a wrongful act prevents one of the parties to a contract from performing it. He may be sued for damages for this wrongful act and that the contract did not conform to the statute is no defense to him.

EXAMPLE

Jackson verbally contracted with Jones to sell a large quantity of lumber for $5000. Stanfield learned of this contract, offered to furnish Jones the lumber at a lower price and guaranteed to protect Jones if he would break his contract with Jackson. Jackson sued Stanfield for causing Jones to break this contract and Stanfield defended on the ground that the contract was not enforceable because it did not conform to the requirements of the Statute of Frauds. Jackson was allowed to recover damages against Stanfield, for the defense was personal with Jones and extended only to the immediate parties to the contract. Jackson vs. Stanfield, 137 Ind. 592.

**255. Note or Memorandum in Writing.** One of the methods of conforming to the requirements of the Statute of Frauds is to have a written note or memorandum of the bargain signed by the party to be charged, or by some agent in his behalf. This note or memorandum need not be a formal document. It is sufficient

if it consists of an admission of the existence of the contract signed by the party, stating the names or descriptions of the parties, the price, and the goods sold. This memorandum may be either retained by the party signing it, or delivered, and in either event it is sufficient.

The following is a sufficient memorandum:

"I have this day agreed to buy of George Underwood 700 bushels of spring potatoes, to be delivered at my warehouse within sixty days, for which I will pay sixty cents a bushel. Signed, Henry Coe."

In commercial usage it is customary in important transactions to use a more formal instrument known as a Bill of Sale, which in addition to complying with the requirements of the Statute of Frauds also contains provisions warranting the seller's title and right to possession. The buyer usually records this instrument with the clerk of the city, village, or town so as to protect himself against a wrongful act of the seller in subsequently reselling the same property to another person.

BILL OF SALE

**Know All Men by These Presents,** *That R. E. Parker, of the City of Chicago, in the County of Cook, and State of Illinois, party of the first part, for and in consideration of the sum of One Hundred and Fifty Dollars, lawful money of the United States of America, to him in hand paid, at or before the ensealing and delivery of these presents, by F. S. Blair, of the second part, the receipt whereof is hereby acknowledged, has granted, bargained, sold, and delivered, and, by these presents, does grant, bargain, sell, and deliver, unto the said party of the second part, all the following goods, chattels, and property, to-wit: One Remington Typewriter, No.* 14678.

**To Have and to Hold** *the said goods, chattels, and property unto the said party of the second part, his heirs, executors, administrators, and assigns, to and for his own proper use and behoof, forever.*

**And** *the said party of the first part does vouch himself to be the true and lawful owner of the said goods, chattels, and property, and have in himself full power, good right, and lawful authority, to dispose of the said goods, chattels, and property, in manner as aforesaid. And he does, for himself, as well as for his heirs, executors, and administrators, covenant and agree to and with the said party of the second part, to warrant and defend the said goods, chattels, and property to the said party of the second part, his executors, administrators, and assigns, against the lawful claims and demands of all and every person and persons whomsoever.*

**In Witness Whereof,** *I have hereunto set my hand and seal, the 24th day of July, in the year one thousand nine hundred fifteen. R. E. PARKER.* [Seal]

*Sealed and delivered in the presence of*
*L. MITCHELL.*

**256. Receipt and Acceptance of Part of Goods.** One manner in which the requirements of the Statute of Frauds may be satisfied, is by the receipt and acceptance of a part of the goods sold by the buyer, as has been previously stated. If this be done the contract will be enforced regardless of the non-existence of a written memorandum. Acceptance of goods may precede, be contemporaneous with, or be subsequent to receipt of the goods, and both may be subsequent to the contract of sale.

EXAMPLES

1. Dean agrees to sell Sauer some wheat in a bin. Subsequently Dean separates the proper amount of wheat from the remainder of the mass and delivers it to Sauer, who accepts it. Here the receipt and delivery are subsequent to the contract to sell. After they have taken place the contract is an executed sale. If Sauer had received and accepted only part of the wheat which he agreed to buy, the contract would have been enforceable by either party.

2. If in the above example Dean had delivered the wheat in bags at Sauer's warehouse, in the absence of Sauer, the latter's acceptance might take place by act as well as word. Thus, if after the delivery Sauer had not communicated with Dean, nor even examined the wheat, but had exercised an act of ownership as by reselling, or agreeing to resell it, to Gray, this act would be deemed an acceptance and he could not later refuse to keep the wheat or pay for it.

If the receipt and acceptance of a *part* of the goods be relied upon to satisfy the requirements of the statute, it must be shown that the part received was not merely a sample to indicate the general nature of the commodity, such as merchants frequently deliver free of charge as an advertisement, but that the part received actually diminished the bulk, that is, the quantity of the goods subsequently to be delivered to the buyer.

**257. Part Payment.** As previously stated, another manner in which the requirements of the Statute of Frauds may be satisfied is by the payment of a part of the price by the buyer, or the giving of something in earnest to bind the bargain. No specific amount is required to be paid, but it does require payment, and a mere promise to pay is insufficient. The payment need not, however, be in money; it may be made in other property.

EXAMPLE

Edgerton bought 975 pounds of milk cheese of Hodge to be delivered when he wanted it. After the bargain was made Hodge wrote Edgerton stating

that if he wished the cheese kept for him he must send fifty dollars in part payment. Edgerton immediately mailed his check for that amount, but the price of cheese advanced meanwhile and Hodge returned the check and sold the cheese to other parties. Edgerton was without remedy because the contract was not in writing, and there had been no part payment because Hodge did not accept the money, or its equivalent. Edgerton vs. Hodge, 41 Vt. 676.

## REVIEW QUESTIONS

1. Miller, owning a quantity of logs in a mill-pond adjacent to his mill, made a verbal contract with Carpenter to manufacture the logs as follows: (1) To cut them so far as possible into dimension stuff of dimensions to be furnished by Carpenter; (2) the balance, so far as practicable, into common lumber; (3) whatever was left into shingles; for all of which Carpenter agreed to pay a specified price per thousand feet. Miller fully performed his part of the contract, and the amount due under (1) was $3,000; under (2) $1,500, and under (3) $1,000. Carpenter declined to accept or pay for any of it, and Miller sued him on the contract. May he recover? If so, how much?

2. Mercy verbally sold to Winslow (1) all of the hay which would grow on his farm for the coming season, for $100; (2) all of the pine lumber on his farm, for $800; (3) all the wheat growing on his farm, for $400; which prices Winslow agreed to pay. Later Mercy cut the hay and harvested the wheat, storing it in his barn to be later delivered to Winslow. A fire destroyed the barn and its contents and damaged the standing timber. Who bears the loss? Why?

3. Suppose, in the above question, eliminating the element of the fire, that Mercy had offered to deliver the hay and wheat, and that Winslow had refused to accept them. Would Mercy have had any remedy? What?

4. Loomis examined barrel hoops at Potter's factory and agreed orally to purchase some for $200. Loomis told Potter to deliver them to his steamer Winnebago for transportation. Potter delivered them to Loomis' steamer. The Winnebago was destroyed on Lake Michigan with her cargo. Potter sued Loomis for the price, and Loomis defended on the ground that the contract was not in writing. May Potter recover? Why?

5. Mason wrote to Jarvis, "Please quote price of brass hoops." Jarvis later wrote Mason a letter in regard to other matters and added an unsigned post-script as follows: "P. S. Will make price of two tons of hoops, immediate delivery, 17 cents lb." Mason by telephone accepted the offer, ordering two tons. Jarvis acknowledged the telephone conversation by a letter stating that he would ship the hoops at once. Later he refused to deliver the hoops on the ground that the contract was not in writing. May Mason recover for breach of contract? Why?

6. Archer and Conklin drew a bill of sale whereby Archer agreed to buy, and Conklin to sell, five tons of coal for $8 a ton. Archer received the coal and, when Conklin sued him for $40, Archer attempted to show that he and Conklin had orally agreed at the time of the contract that the price of the coal should be only $6 a ton. May he do so? Why?

## CHAPTER XXV

## TRANSFER OF TITLE

**258. Introduction.** The object of a sale of, or contract to sell, goods is to transfer the title or property in them from the seller to the buyer. The time at which the transfer of property rights takes place is important as between seller and buyer, for several reasons. After the title has been transferred to the buyer he must bear any risk of loss,* and is also entitled to the benefit of any gain or increase. He may again transfer the title to another, even against the objection of the original seller, or the goods may be taken by his creditors to satisfy his debts through the medium of an execution and levy. He must also pay the price to the seller.

Before the title to personal property which is the subject matter of a sale has been transferred, the goods still belong to the seller and he bears the risk of loss, receives the benefit of increase, holds the goods subject to the rights of his own creditors, and, if the buyer refuses to accept them, is limited to an action for damages for breach of contract, instead of being able to recover the contract price. Or he may transfer a valid title in the goods to a third person, which will be valid even against the original buyer, though should he do so the buyer may recover the damages which he has sustained by reason of the seller's breach of contract.

While it is apparent that it is of the utmost importance to discover when the title to the goods has been transferred from the seller to the buyer, the determination is not always a simple task. A sale is the result of a contract relation, and as is true with all contracts the intention of the parties is the controlling

* If after title has been transferred to the buyer, together with the risk of loss, the buyer should allow the seller to retain possession of the goods, the latter could not of course wantonly destroy them, nor could he be relieved from loss because of the transfer of title if his negligence resulted in their destruction or injury. The duty which devolves upon a custodian of another's goods is discussed under the subject of Bailments.

factor. Whenever this intention is indicated, it alone will determine the time of transfer. If it is clear that the parties intended that title should pass at a certain time in the negotiations, title will be considered to have passed at that time. But if they did not intend that it should have passed, it will be deemed to remain in the seller.

It is not always an easy task, however, to determine the intention of the parties from their words and conduct. In the majority of instances the parties to a sale say nothing about the time of the transfer of title, and if disputes arise in these instances the intention of the parties must be determined from their acts and conduct and the circumstances of the particular sale.

**259. Ascertained and Unascertained Goods.** Various rules are applied in determining the intention of the parties, and the application of these rules depends upon whether the goods which are sold, or contracted to be sold, are ascertained or unascertained. If the goods which are the subject of the sale are specific, and designated so that both the seller and buyer know exactly what goods are the subject of the sale, and no others will suffice, the sale is one of ascertained goods. On the other hand, if the goods are merely described generally and any goods of like character will suffice, or if a future act of the parties is necessary to designate them, the sale is of unascertained goods.

EXAMPLES

1. Cook contracts to sell to Brown 10,000 first-class vitrified bricks, Brown agreeing to pay $40 a thousand on delivery. This is a contract to sell unascertained goods, for no particular body of bricks is within the contemplation of the parties.

2. Cook contracts to sell to Brown all the bricks in his warehouse in South Bend, being 10,000, more or less, which Brown agrees to buy at an agreed price for the lot. This is a contract to sell ascertained goods, for a particular body of goods is within the contemplation of the parties.

**260. Rules in Sales of Ascertained Goods.** *Rule One.* In case there is an unconditional contract to sell specific goods, in a deliverable state, the property in the goods passes to the buyer when the contract is made. It is immaterial whether the time of payment, or time of delivery, or both, be postponed.

EXAMPLE

1. Tarling on January 4th agreed to buy a stack of hay of Baxter, to be paid for on February 4th, and to remain on Baxter's land, where it then stood,

until May first, when Tarling was to remove it. On January 20th the hay was destroyed by fire, and Tarling suffered the loss, for title was deemed to have been transferred when the contract was made. The goods were specified and ascertained, although both payment and delivery were postponed. Tarling vs. Baxter, 6 B. & C. (Eng.) 360. The parties could, however, by express agreement, have postponed the time of the transfer of title, in which event the seller would have continued to bear the risk of loss.

*Rule Two.* When the contract is to sell specific goods, if something remains to be done by the seller to put them in a deliverable state, the property in them is not transferred to the buyer until this is done and notice given. Similarly, if the seller is required to measure or weigh the goods for the purpose of ascertaining the amount due, the title is not considered to be transferred until this is done.

EXAMPLES

1. Brown made a written agreement with Furniss, selling the latter a one-half interest in the steam boat *Rhode Island*, agreeing to fit out the boat in a suitable manner for her to proceed from New York to the Pacific. After the contract and before the boat was entirely fitted out it was destroyed by fire. Brown was compelled to suffer the loss. Decker and Brown vs. Furniss, 14 N. Y. 614.

*Rule Three.* If ascertained goods are delivered to the buyer on trial or on approval, the property in them passes to him, (1) when he signifies his approval or (2) if he does not return them within a reasonable time.

The parties may, however, make the sale a transaction known as a "sale or return," by which the goods are delivered to the buyer with the understanding that the property is to pass to him immediately, but that he may afterwards return the goods if he sees fit, in which event the title is in the buyer until he returns the goods. Such a sale is an exception to the general rule and exists only where the parties have made it clear that they intended such a result to follow.

EXAMPLE

1. Fairfield made a written contract with the Madison Manufacturing Company for the purchase of a reaper, one of the terms being that the reaper should be delivered to him for a fair trial and that if he did not find the machine as represented he should return it. He tried it for two days and then notified the seller that it was unsatisfactory, and that he would return it to any place the seller designated. The seller suffered the loss caused by the destruction of the reaper. Fairfield vs. Madison Manufacturing Company, 38 Wis. 347.

**261. Unascertained Goods.** *Rule One.* When the seller purports to sell, and the buyer to buy, an undivided share in a specific mass of goods, the property in a proportionate share of the mass is deemed to have been transferred, even though the number, weight, and measure of the goods in the mass is undetermined.

This is known as a sale of fungible goods, being goods such as oil, grain, or molasses, which is a uniform mass, of which a part is sold. At the making of the contract the property in a part of the mass is immediately transferred without its separation and the buyer becomes an owner in common of the mass.

*Rule Two.* When the goods which are sold, or contracted to be sold, are unascertained, the property in them is transferred from the seller to the buyer at the time at which the goods are unconditionally appropriated to the contract.

Edwards in Ohio ordered a quantity of calf and buff shoes from Smith in Massachusetts. Smith manufactured the shoes according to specification and delivered them to the railroad for transportation. In a contest between creditors it was decided that the title was transferred at the time of delivery to the railroad, Smith having then complied with the conditions of the contract. Smith vs. Edwards, 156 Mass. 221.

*Rule Three.* If the contract of sale by its express terms requires the seller to deliver the goods to the buyer, or at a particular place, or to pay the freight or cost of transportation to the buyer, or to a particular place, the property in the goods is not transferred until the goods have been delivered to the buyer or reach the place agreed upon.

EXAMPLE

Brown ordered 98 tons of coal from McNeal, to be delivered at Brown's wharf at Burlington. McNeal shipped the coal by barge, the barge sinking at night while anchored alongside the wharf in Burlington before being unloaded. McNeal suffered the loss, because there had been no delivery and the title and risk of the goods were still in the seller. McNeal vs. Brown, 53 N. Y. L. 617.

**262. Title to C. O. D. Shipments.** No uniform rule exists regarding C. O. D. (Collect on Delivery) shipments, or shipments in which the railroad, postal department, or express company, is instructed by the seller to collect on delivery, and

not to surrender the goods to the buyer until the freight charges and purchase price have been paid to the carrier. In Georgia, Iowa, Missouri, Vermont, Indiana, Massachusetts, and North Carolina, the seller retains title until the price has been paid. In the majority of the states, however, the property is considered to have been transferred to the buyer immediately upon delivery to the transportation company, even though the buyer cannot receive the goods until he has paid the price. The latter is the view adopted by the Uniform Sales Act. The law applicable in the state where delivery to the carrier is made determines the matter.

**263. Necessity of Delivery.** As between seller and buyer the delivery of the goods sold is not necessary to transfer the title. Even though the goods are retained by the seller the risk of loss is frequently borne by the buyer. But if no bill of sale has been given and recorded the delivery of the goods is of the utmost importance when disputes arise regarding the rights of third persons. Suppose that Ames has sold all the hay in his barn to Bates, but retains the hay. Bates bears the risk of loss, for as between him and Ames the property has been transferred, although the seller has retained possession. But if Ames, while still in possession of the goods, resells them to Call, who carries them away, or borrows money from Dale, then either Call or Dale may acquire a title which is superior to that of Bates. This is because the sale between Ames and Bates is considered fraudulent as against third parties who acquire rights under the assumption that the goods belong to Ames, the seller, relying on Ames' possession.

Two rules exist to protect third parties against such acts of the buyer who, by leaving the seller in possession of the goods, creates a situation which results in damage. The first applies to subsequent purchasers of the goods in good faith, such as Call above, and the second to the rights of creditors of the seller, such as Dale above.

**Subsequent Purchasers.** If a buyer leaves the goods purchased in the hands of a seller and the seller wrongfully sells and delivers the goods to a third party, this subsequent purchaser acquires a title in them superior to that of the first

buyer, who allowed the seller to retain possession. In favor of the subsequent purchaser, the original sale is void because of the failure to have a delivery. The Uniform Sales Act, Section 25, contains a clear statement of the law on this point as follows:

> When a person having sold goods continues in possession of the goods, the delivery or transfer by that person of the goods under any sale, pledge, or other disposition thereof, to any person receiving and paying value for the same in good faith and without notice of the previous sale, shall have the same effect (that is, as to the rights of the last purchaser) as if the person making the delivery or transfer were expressly authorized by the owner of the goods to make the same.

**As to Creditors.** Ordinarily creditors may sieze any goods belonging to a debtor. If he holds possession of the goods and claims that someone else owns them, it is presumed that the claim is fraudulent. In most states this evidence is only presumptive, and if the debtor can prove that the goods have already been sold in good faith, the tale will stand.*

EXAMPLES

1. Ingalls bought from Lougee 21 bales of wool, which were left for the time being in Lougee's warehouse. While they were there, the sheriff took possession of them in behalf of some of Lougee's creditors. Ingalls proved that he had bought and paid for the wool in good faith and that he had not removed it at once on account of its bulk, but that he would have done so within a short time. The court allowed Ingalls to recover the wool from the sheriff, the law being that while the transaction was presumptively fraudulent he had proved that it was not so in fact, and could therefore assert his title in the goods. Ingalls vs. Herrick, 108 Mass. 351.

2. A sale in which the seller keeps possession is not absolutely void as against creditors, but is merely presumptive evidence of fraud. Martindale vs. Booth, 3 B. & A. (Eng.) 498. McKibben vs. Martin, 64 Pa. St. 352.

The safe business practice, when for any reason the seller is allowed to retain possession of the goods sold, is for the buyer to require a formal bill of sale, and to record the bill of sale with the proper officer, usually the town, city, or village clerk. This serves to give notice to all subsequent parties, who cannot then

*In other states the same rule is applied in regard to creditors as is applied to protect innocent subsequent purchasers, that is, that the buyer loses all rights as against third parties by allowing the seller to retain possession. These states are California, Colorado, Connecticut, Idaho, Illinois, Iowa, Kentucky, Maryland, Missouri, Montana, Nevada, New Hampshire, Oklahoma, South Dakota, Utah, Vermont and Washington.

claim to have innocently and ignorantly relied upon the seller's retention of possession as evidence that he was still the owner of the goods.

**264. Sufficiency of Delivery.** The buyer may avoid all danger of losing his rights in the goods, either to subsequent purchasers or to creditors of the seller, if he insists upon the goods being delivered to him. The requisites essential to a valid delivery depend upon the nature of the article sold. If the article is of extreme bulk and cannot be removed, the buyer must enter into active, open, and notorious possession and perform acts which will indicate generally that he and not the seller is the owner of the goods. The execution of a bill of sale constitutes such an act.

**265. Conditional Sales.** Not only does the buyer, in actual business, often allow the seller to retain possession of the goods after title has been transferred, but even more often is the buyer allowed to enter into possession of the goods before the title has passed. This is accomplished by a *conditional sale*, the parties contracting that the title shall not be transferred until the buyer has paid the price, which is often to be paid in installments. Pianos, sewing machines, and typewriters are often sold by contracts of conditional sale. The rule of the common law was that the buyer in such a case acquired no title which he could transfer even to an innocent purchaser from himself for value, and that the seller could always regain the goods no matter into whose hands they might have passed. This rule has been quite generally changed by statute in the several states.* These statutes usually provide that conditional sales are void against any innocent purchaser for value from a buyer who has been placed in possession of the goods, unless the contract of conditional sale is recorded in writing in a specified public place, usually the office of the town, city, or village clerk. As between

* Such statutes exist in Alabama, Arizona, Colorado, Connecticut, Florida, Georgia, Iowa, Kansas, Maine, Minnesota, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Ohio, Oklahoma, South Carolina, Texas, Vermont, Virginia, Washington, West Virginia, Wisconsin and Wyoming. In Tennessee the only requirement is that conditional sales must be written to be valid as to third persons. In Massachusetts the recording statute applies only to sales of household furniture.

the buyer and the seller, the parties may contract validly for the retention of the title by the seller as security for the purchase money, but innocent parties who rely on the possession of the goods under such transactions as an apparent evidence of ownership and title will not be allowed to suffer by such agreements, if secret; if they are recorded as public documents, all persons are presumed to know of them.

**266. A Chattel Mortgage** from its form would appear to be a form of conditional sale, but it is in reality only security for a debt. The parties to it are the *mortgagor*, who is the debtor who pledges his property to secure a debt, and the creditor, who is called the *mortgagee*. It forms a popular means of securing a debt by a pledge of personal property, and does not constitute a sale of the property. The instrument, known as a chattel mortgage, is a formal document by which the owner of property agrees that another person shall hold the title to the property as security for the payment of a debt. It provides that upon the payment of the debt, the title shall revest in the original owner, the mortgagor.

So far as the parties themselves are concerned, chattel mortgages may be either oral or written. But in order to prevent fraud upon third persons, by allowing one person to hold the title to goods as security, and another to have possession of the goods, the statutes of the various states provide that they must be formally executed and registered or recorded with some designated public officer, usually the town clerk. The statutes usually provide that a chattel mortgage shall have no effect against innocent third parties unless it is executed and recorded in the manner provided by law.

The mortgagee's rights depend largely upon the statutes of the state in which the mortgage is made, and also upon the conditions of the instrument itself. The mortgagee is frequently given the right by the instrument to enter the premises of the mortgagor at any time and take possession of the goods upon the failure of the debtor and mortgagor to pay the debt at its maturity, or if he has reason to believe that some act of the mortgagor has imperiled his security. Regulations are usually provided for the advertisement and public sale of the property so

taken, and unless the mortgage expressly permits it it cannot be sold at private sale.

EXAMPLE

Ames borrowed money from Bates, and to secure the debt gave Bates a chattel mortgage on all his cattle. This was recorded with the town clerk two weeks later, on June 1. On May 25, Call, a creditor of Ames, levied upon three cows, as did Dale, another creditor of Ames, on June 5. Call could claim the cows as against Bates, but Dale could not, for the recording of the mortgage had preceded his levy.

## REVIEW QUESTIONS

1. A contracted to sell to B 100 bushels of wheat, to be put up by A in sacks furnished by B, and subsequently to be called for by B. B paid the price at the time of the bargain. Thereafter B sent A enough sacks to hold the wheat, and A at once began to fill them. He completely filled and tied up a quarter of the sacks. A quarter of the sacks he partially filled. He was then interrupted and shortly after became bankrupt. The creditors of A claimed the wheat, as did B. Who was entitled to the wheat? Which part?

2. A agreed to sell to B his drove of cattle, with the exception of five fat calves which A was to select to keep. B paid one-half the purchase money down, and was to call the next day for the drove and pay the balance. That night the cattle were destroyed by a flood. Does the loss fall on A or B? Why?

3. At Mahoney's request Fisher sends a stove to Mahoney, to be returned if not found satisfactory, no specified time being given in which the stove must be returned. Mahoney keeps the stove a year without offering to return it, and then, when a bill is presented for the stove, he says it is not satisfactory, that he has used it only once, and had stored it in his attic ready for Fisher to get it any time, and now offers to pay a delivery man to return it to Fisher. Has the sale been completed, and can Mahoney be compelled to pay for the stove?

4. X sells B 250 bags of coffee, marked and designated, but X agrees to weigh the bags in order to ascertain the total price, the sale being by the pound. Has title passed to B?

5. A sold B an automobile for cash, but as B had no place to keep it, A agreed that it might be left in his garage for a few weeks until B had time to build a garage. During this time B used the machine frequently, coming to A's house to get it and leaving it there when it was not in use. A did not use the automobile at all after the sale to B, but later sold and delivered it to X, who paid cash and had no notice of the previous sale to B. As A was financially worthless B sued X to recover the automobile. May he recover? Why?

# CHAPTER XXVI

## TRANSFER BY BILLS OF LADING AND WAREHOUSE RECEIPTS

**267. Introduction.** The ordinary conception of a sale assumes that it includes the delivery of the goods by the seller to the buyer. It is not always desirable, however, or even possible, to effect a physical transfer. In such a case a constructive delivery can be made. When goods are in the hands of a common carrier, or a warehouseman, it is important to know how they may be transferred from seller to buyer, and just when such transfer takes place. One who holds the goods of another is called a *bailee.*

It has long been the mercantile custom for the bailee, if a carrier or warehouseman, to issue to the owner a receipt for the goods which will entitle the owner to receive the goods upon its presentation. A receipt from a carrier is called a bill of lading; one from a warehouseman, a warehouse receipt. Both are commonly known as documents of title, and are governed by the same rules of law. In the warehouse receipt the bailee usually promises to deliver the goods to the person who has deposited them. In the bill of lading the carrier ordinarily promises to deliver the goods to the person to whom they were shipped, who is called the consignee. In the following discussion reference will be made principally to bills of lading, for convenience of treatment, but it is to be noted that the same rules are applicable to warehouse receipts.

**In Two Forms.** Bills of lading are issued in two forms. The first, called a *straight* bill of lading, names a particular person to whom the goods are to be delivered. The second type, which is called an *Order* bill of lading, and is negotiable, states that the goods will be delivered to some particular person, or to his order.

## Straight Bill of Lading (Not negotiable)

C.B.&Q. & Big 4 **Railroad Company**

STRAIGHT BILL OF LADING—ORIGINAL—NOT NEGOTIABLE.

Shipper's No. 1246

Agent's No.

RECEIVED, subject to the classifications and tariffs in effect on the date of issue of this Original Bill of Lading, at Kearney Nebr. Jan 3, 1916 FROM Benj. H. Patterson

the property described below, in apparent good order, except as noted (contents and condition of contents of packages unknown), marked, consigned and destined as indicated below, which said company agrees to carry to its usual place of delivery at said destination, if on its road, otherwise to deliver to another carrier on the route to said destination. It is mutually agreed, as to each carrier of all or any of said property, over all or any portion of said route to destination, and as to each party at any time interested in all or any of said property, that every service to be performed hereunder, shall be subject to all the conditions, whether printed or written, herein contained (INCLUDING CONDITIONS ON BACK HEREOF) and which are agreed to by the shipper and accepted for himself and his assigns.

The rate of freight from _____ to _____ Is In Cents per 100 lbs.

| If ... Times 1st | If 1st Class | If 2d Class | If Rule 2B | If 3d Class | If Rule 2G | If Rule 2S | If 4th Class | If 5th Class | If 6th Class | If Special per ... | If Special per ... |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | | | |

(Mail Address—Not for purposes of Delivery)

Consigned to D. F. Sloyde & Co.

Destination, Crampaign State of Ills. County of

Route, Car Initial Car No.

| No. PACKAGES | DESCRIPTION OF ARTICLES AND SPECIAL MARKS | WEIGHT (Subject to Correction) | CLASS OR RATE | CHECK COLUMN |
|---|---|---|---|---|
| 1 | piano | 425 | | |

If charges are to be prepaid, write or stamp here "To be Prepaid."

Received $ _____ to apply in prepayment of the charges on the property described hereon.

Agent or Cashier

Per _____ (The signature here acknowledges only the amount prepaid.)

Charges Advanced:

$ _____

Ben. H. Patterson Shipper.

Per _____

H. Safford Agent

Per B B

(This Bill of Lading is to be signed by the shipper and agent of the carrier issuing same.)

UNIFORM BILL OF LADING—Standard form of Straight Bill of Lading approved by the Interstate Commerce Commission by Order No. 787 of June 27, 1908.

## Order Bill of Lading (Negotiable)

Heading only

Uniform Bill of Lading—Standard Form of Order Bill of Lading Approved by the Interstate Commerce Commission by Order No. 787, of June 27, 1908

C. & E. I. **Railroad Company**

**ORDER BILL OF LADING—ORIGINAL**

Shippers No. 1247

Agents No. _____

**RECEIVED**, subject to the classifications and tariffs in effect on the date of issue of this Original Bill of Lading, at Chicago Ills. July 23, 1915 from Lyons & Carnahan the property described below, in apparent good order, except as noted (contents and condition of contents of packages unknown), marked, consigned and destined as indicated below, which said Company agrees to carry to its usual place of delivery at said destination, if on its road, otherwise to deliver to another carrier on the route to said destination. It is mutually agreed, as to each carrier of all or any of said property over all or any portion of said route to destination, and as to each party at any time interested in all or any of said property, that every service to be performed hereunder shall be subject to all the conditions, whether printed or written, herein contained (including conditions on back hereof) and which are agreed to by the shipper and accepted for himself and his assigns.

**The surrender of this Original ORDER Bill of lading properly indorsed shall be required before the delivery of the property. Inspection of property covered by this bill of lading will not be permitted unless provided by law or unless permission is indorsed on this original bill of lading or given in writing by the shipper.**

*The Rate of Freight from* _____

*to* _____ *Is in cents per 100 Lbs.*

| If ... Times 1st | If 1st Class | If 2d Class | If 3d Class | If 4th Class | If 5th Class | If A Class | If B Class | If C Class | If D Class | If E Class | If Special per ... | If Special per ... |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | | | | |

It will be observed that the only material difference between these two forms is that in the negotiable type the goods are consigned "to order of" the consignee, while the words of negotiability are omitted in the straight, or non-negotiable bill. There

is also added to the negotiable type a provision requiring its surrender properly indorsed before delivery of the goods will be made.

**268. Methods by which the seller retains possession.** When goods are shipped on a straight bill of lading, the title in them is in the buyer. If the seller wishes to retain possession, he should at the time of shipment secure from the railroad an order bill of lading. This order bill of lading may be made out in one of three ways.

1. The seller may name himself as consignee, and hold the bill of lading until the buyer pays him or pays someone else for him. He will then indorse the bill of lading and deliver it to the customer.

2. The seller may name the buyer as consignee, or may name himself as consignee and immediately endorse in favor of the buyer, but instead of sending the bill of lading to the buyer, send it to some bank or other collecting agency in the buyer's city, with a draft upon the buyer attached and with instructions to deliver the bill of lading to the buyer only upon payment of the amount of the draft.

3. The seller may name as consignee a third person, say a bank in the city of the buyer, and send the bill of lading to the bank with instructions to release it to the buyer upon his payment of a certain sum of money.

The second plan named is the one most commonly adopted and is the best. The first plan is desirable only when the consignee is unknown at the time of shipment, as in case of produce shipped to be sold *en route* or at destination. The third plan is undesirable ordinarily because it places the collecting agent in apparent temporary possession.

All three plans are alike except that the consignee is different in each case. The object in each case is the same — each is a plan by which the seller keeps possession until he gets his money.

In case of goods stored, the same three plans can be followed, but the evidence of title is in this case a warehouse receipt instead of a bill of lading.

**269. Transfer of Title by Means of Documents of Title.** Not only are bills of lading and warehouse receipts used in commerce to protect the seller as to the purchase price, but they are further used as a means by which to transfer the title to goods while they are in transit or stored in a warehouse. A buyer in New York may purchase grain of a seller in North Dakota. While this grain is being conveyed to New York, or after it has reached New York and is stored in a warehouse, the seller, to whom title has passed, may wish to dispose of it. If a negotiable receipt has been issued by which the bailee has promised to deliver the grain to the buyer, or to his order, he may readily dispose of it without ever receiving the grain. He does this by negotiating the document of title.

When goods are shipped by rail, title passes at the time of delivery to the transportation company unless the shipper reserves the right of disposal, as by having the bill of lading made to the order of himself or his agent.

If the shipper reserves the right of disposal, title passes only when he disposes of it to the buyer, which is usually done by a transfer of the bill of lading itself.

If it can be proved from the original contract that the intention of the parties was that title should pass to the buyer at once, this result will follow.

**270. Parties Who May Negotiate.** There are two classes of persons who may negotiate a bill of lading so as to transfer the interest and title in the property itself to another. These are (1) the owner of the bill of lading, and (2) a person who has been intrusted with it by the owner, in case the form is such that it may be transferred by mere delivery. Neither a thief nor a finder of lost documents of title can transfer them so as to give a valid title, even to an innocent purchaser for value.

EXAMPLE

Poor, residing in Superior, is the purchaser and consignee of goods in transit, for which he has received a bill of lading naming him "or order" as consignee. He indorses the same in blank and sends it to Cook in Milwaukee to sell the goods for him for $600. Instead Cook sells them to Jones, an innocent purchaser for value, for $400, and absconds with the proceeds. Poor cannot

reclaim the goods from Jones, or even prevent the railroad company from delivering them to Jones on presentation of the document of title, for Cook was given the authority to transfer the document of title and the fact that he violated the terms of that authority is not the fault of Jones.

**271. Bills of Lading Which May Be Transferred.** All bills of lading and warehouse receipts may be transferred, but only by means of negotiable receipts can the owner transfer the property and title in the goods without further act. If a "straight" bill of lading, or non-negotiable document, be sold and transferred, the buyer does not thereby secure the title to the goods. The bailee may still deliver them to the original consignee, should he demand them. The purchaser of such a "straight" receipt may, however, protect his rights by notifying the bailee that he is the holder of the document of title and has the title to the goods. After such notice the bailee cannot, without incurring liability to the latest purchaser, deliver the goods to the original consignee.

Common carriers have at times sought to destroy the negotiable quality of order bills of lading by marking them across their face "non-negotiable." There has been much difference of opinion in the courts of the various states regarding the effect of this practice. Section 30 of the Uniform Sales Act states that if by its form the receipt was negotiable aside from these words, it will continue so in spite of them.

**272. Rights of Purchaser of Negotiable Bills.** The purchaser of a negotiable bill of lading or warehouse receipt receives the right to demand a delivery of the goods by the bailee in whose custody they have been placed. Furthermore, he not only takes the title in the goods which the seller has, but he secures a valid title if he be a purchaser for value without notice even though the seller's title was voidable. He can not, however, acquire title except from an owner, and in this respect his rights are less than those of a buyer of negotiable paper.

EXAMPLE

Senn, a wholesale dealer, shipped merchandise by the Bell Central Railroad to Poor, a grocer in Muskegon, who had misrepresented his assets and financial responsibility to Senn. Senn sent the bill of lading in the form of a negotiable receipt to Poor, who immediately sold it to Tyson, an innocent

purchaser, for value. Before this sale to Tyson, Senn could have reclaimed the goods and avoided the sale to Poor, because of Poor's fraud. After the sale he can only sue Poor for fraud, but cannot reclaim the goods from Tyson, who alone can secure them from the railroad company.

**273. Limitations of Rights of Purchaser Against Bailee.** Although it is the general rule that the purchaser of a bill of lading has the right to receive the goods themselves from the bailee, he cannot receive them if the bailee hasn't the goods or if the shipper was not the true owner. If the bailee never had the goods, or parted with them, or they were destroyed, the bailee is answerable in damages. If the seller of the bill of lading was not the true owner of the goods, he is answerable in damages.

## REVIEW QUESTIONS

1. White ordered from Jones in Chicago a dozen typewriters, to be charged to his account. Jones wrote: "Order received and will ship at once." Jones then delivered the typewriters to the railroad, but in the bill of lading named himself as consignee, and retained the bill of lading. While the typewriters were on the way to White, Jones stopped them and sold them to Lewis, delivering the bill of lading. May White, claiming that the goods were his property from the moment of shipment and that Jones no longer had title to sell, reclaim the goods from Lewis? Why?

2. In response to a written order from Bates, Ames shipped goods consigned to the order of Bates. Ames then attached the bill of lading to a sight draft for the purchase price and mailed both documents to Bates with a letter requesting Bates to pay the draft, or to return both documents at once. Bates did not pay the draft, but with the bill of lading obtained the goods from the railroad company and sold them to Call for value. Ames attempts to reclaim the goods from Call. May he do so? May Ames recover from the railroad company? May Ames recover from Bates?

3. Murphy was a lawyer in Milwaukee. Logan in LaCrosse sent him a typewriter to try for thirty days and also sent him for examination and for a legal opinion a negotiable bill of lading for some apples in transit from St. Paul to LaCrosse. The bill of lading was indorsed in blank by Logan. Murphy at once sold both the typewriter and the bill of lading to Jones, an innocent purchaser for value. Both Jones and Logan now claim the right to receive the apples from the railroad company. Who is entitled to the apples? May Logan reclaim the typewriter from Jones? Why?

4. If Morrison offered to sell you a negotiable bill of lading made to "Morrison, or order," as the consignee, at a fair price, indorsed by him, what further inquiry, if any, would you make in order to safeguard your rights? Would you pursue any different course if the bill of lading were in the form of a "straight" receipt?

5. Gordon & Co. are wholesale grocers in Milwaukee. Waters is a retail merchant in Galena. Waters by telephone orders ten barrels of sugar at $30 a barrel from Gordon & Co. to be shipped to him in two weeks. Gordon & Co. deliver the sugar to the office of the Northwestern Railway Company on the same day that the order is given and receive a bill of lading with Waters, or order, named as the consignee, which they retain. While the sugar is still at the depot, Gordon & Co. are declared bankrupt and their creditors, through a trustee, claim that the sugar is still their property. Waters also claims it. Who has title to the sugar? Why?

## CHAPTER XXVII

## WARRANTIES

**274. A warranty** is a statement by the seller, given as a fact either express or implied. It is an express warranty if it is a statement of fact made at the time of or before the sale, which has a natural tendency to induce the buyer to purchase the goods, and upon which he does rely in purchasing the goods. It is not a condition of the contract which must be performed by the seller before a liability arises on the part of the buyer to pay the price, but it is in the nature of a separate, collateral promise, and if broken gives rise to an action for damages for its breach.

**275. Express and Implied Warranties.** Warranties may be either express or implied. They are express warranties if the seller at the time of, or prior to, the sale makes statements regarding the thing sold which are inducements to the other party to purchase and which are relied upon by him. They are implied warranties if they are not made by express language, but depend for their existence upon the entire surroundings of the transaction and the general nature of business dealings of that kind, being then implied by law and fact.

EXAMPLES

**Condition precedent.** Ames makes Bates the following offer, "For $6000, I will build you an automobile which will run 60 miles an hour on the track at Ormond Beach when you try it out." Bates accepts this offer. The attainment of this speed is a condition precedent to any liability on the part of Bates to receive the automobile as his property, and to pay for it.

**Express Warranty.** Call says to Dale, "I will sell you this horse for $125 and warrant him to be sound." Dale accepts this offer, receives the horse and pays the money. The horse is internally diseased; this constitutes a breach of an express warranty.

**Implied Warranty.** Egan sells and delivers to Fair a threshing machine at a fair price. It later develops that Gould is the true owner of the machine and he reclaims it from Fair, who may then sue Egan for damages for breach of an implied warranty, the warranty which such a seller makes by implication

that at the time of the sale he is the owner and has title to the property sold. (The selling of another's goods in this manner also constitutes a criminal offense, the taking of another's goods being larceny and the fraudulent sale being the obtaining of money under false pretenses.)

**276. Nature of Express Warranties.** To be a warranty, the statement of the seller must be the affirmation of a fact and not a mere statement of opinion. Thus a statement as to the value of the thing sold is not a warranty, for value is always a matter of mere opinion. The statement must also be positive and not a mere supposition.

It must also be a statement of such a nature as will in the ordinary course of events be relied upon by the purchaser. A purchaser cannot recover for damages for breach of a warranty against defects which he knew existed at the time of the sale, for he cannot assert truthfully that he relied on the warranty. Nor can he recover for damages for breach of warranty when there was no warranty but he relied upon independent information as to the character of the thing sold.

If a warranty is made at the time of the original contract of sale, it is supported by the original consideration and is enforceable by the buyer. If it is made at a time later than the original sale or contract to sell it must be supported by a new consideration, or it will not be enforceable.

EXAMPLES

1. Jones sells to Murphy a fire-proof safe, saying, "That safe is easily worth $300, for I am told that it will withstand any fire without damage to papers which it contains." Murphy pays $300 for the safe, and in a fire later the safe is damaged so that many valuable papers are destroyed. There is no breach of warranty, for the statement of Jones was a mere matter of opinion.

2. Olson sells Herring a suit of clothes and warrants that it is all wool and will not "shoddy," the promise of Olson as to the quality being one of the inducements that leads Herring to buy the suit. Herring suffers a detriment (the payment of the price of the suit) in reliance on this promise. If, therefore, the suit proves to be not all wool, Herring is damaged upon a warranty which is supported by a sufficient consideration.

3. Ames, a hardware dealer, sells Bates a bath-tub and installs it in Bates' house. A month later Ames says to Bates, "That was a fine bath-tub I sold you; it will not discolor in ten years." Five years later the bath-tub discolors, and Bates sues Ames for breach of warranty. In this case Ames has a good defense in that the alleged warranty was not supported by a sufficient consideration.

**277. Caveat Emptor.** This is a Latin phrase which means, "Let the buyer beware." It has been adopted by the courts as a maxim concerning sales in general, the rule which it represents being that the seller is not liable for defects which the buyer should have discovered had he used reasonable care in examining the article bought. The effect of this rule is to throw the risk of loss on the buyer in case he fails to use due diligence. The buyer has the right, however, to rely upon an express warranty.

In consequence of this rule the buyer should require that all doubtful matters be covered by an express warranty. He may also usually rely upon the implied warranties later enumerated, though in the sale of specific articles examined by the buyer there is no implied warranty except as to the title of the seller.

**278. Implied Warranties.** There are two general classes of implied warranties. There are (1) warranties of title, and (2) warranties of quality.

**Warranties of Title.** In early law there was no implied warranty as to the title of the seller, but it is today everywhere recognized that by the very act of selling the goods the seller represents to the buyer that he nas a good title, and if it later proves that he had not, the buyer may recover damages for breach of this warranty. This is true in all sales except when the situation of the seller is such as to disprove any such representation.

EXAMPLES

1. Dewey sold Burt a horse, which had previously been stolen from Dysart, though both Dewey and Burt were ignorant of that fact. Upon the reclaiming of the horse by Dysart, Burt was entitled to recover damages from Dewey. Burt vs. Dewey, 40 N. Y. 283.

2. Colby, being heavily in debt, transferred his property to Ammidown as a trustee to distribute it among his creditors. Ammidown sold the property as the trustee at a public sale to Cohn, who on discovering that Colby's title had been defective sued Ammidown. He was refused recovery for the reason that no personal warranty of title could be implied against Ammidown, the particular circumstances of the sale plainly showing that he did not intend to assert any title in himself. Cohn vs. Ammidown, 120 N. Y. 398.

**Warranties of Quality.** The rule of *caveat emptor* applies generally to prevent a warranty of quality. There are, however,

five instances in which, in spite of this rule, the law creates an implied warranty of quality on the part of the seller. These are: (1) When the goods are purchased from a manufacturer there is an implied warranty that there are no hidden defects in the goods; (2) when the buyer, relying on the seller's skill and judgment, orders goods for a stated particular purpose, there then is a warranty that the goods are suitable for that purpose; (3) when the goods are ordered by description only, with no opportunity for examination, in which event there is an implied warranty that the goods are reasonably merchantable; (4) in sales of provisions there is an implied warranty that they are fit for food, though in most states this is limited to sales by one who is ordinarily a dealer in such commodities, and this warranty is not applied when the goods were open to ready inspection and their condition apparent to casual examination; and (5) in sales by sample there is an implied warranty that the goods will correspond to the sample.

#### EXAMPLES

1. Randall bought from Newson a buggy and a pole for a team to be used with it. Because of a defect in the pole the team became frightened and ran away causing much damage. It being established that the pole was neither reasonably fit nor proper for the use for which it was ordered, Randall was allowed damages for breach of an implied warranty of quality. Randall vs. Newson, 2 Q. B. (1877) Eng. 102.

2. Drummond sold woolens to Van Ingen by sample, both parties knowing that Van Ingen intended to use them to make suitings. The goods when furnished were according to the samples, but were wholly unsuitable and not merchantable as suitings. When Drummond sued for the price Van Ingen recouped for damages for breach of an implied warranty. Such damages were allowed him, the fact that goods were sold by sample not changing the implied warranty as to merchantability. Drummond vs. Van Ingen, 12 App. Cas. (Eng.) 284.

3. Dounce, who was not a manufacturer, sold Dow a quantity of pig iron. Dow was an iron worker and could have tested the iron easily, but did not. Dow used the iron for construction purposes. It later proved to be very brittle and Dow claimed damages for breach of an implied warranty of merchantability. He was denied recovery because Dounce, not being a manufacturer, could not be presumed to have known the precise quality of the iron or to have warranted it, and also Dow, by using the iron, waived any claim which he might have had. Dounce vs. Dow, 64 N. Y. 411. In this case the doctrine of *caveat emptor* was applied.

4. Bollett saw a carcass of a pig hanging in the shop of a butcher and bought it. Burnby later saw it and inquired the price of the butcher, who informed him that Bollett was the owner. Burnby then bought it of Bollett, and on later discovering that it was wormy and unfit for use, sued Bollett for breach of an implied warranty. He was denied recovery because Bollett was not a dealer in provisions and no warranty was presumed. Burnby vs. Bollett, 16 M. & W. (Eng.) 644.

*Note.*— This is the general rule, although a warranty of wholesomeness is implied in every sale of provisions, without regard to the occupation of the seller, in Michigan and New York.

## REVIEW QUESTIONS

1. Coon, a sewing machine agent, sells a machine to Mrs. Randall, telling her that it is the best machine on the market, and that it runs so easily that it will practically run alone. She finds later that the machine runs harder than other makes, and does not work well; and seeks to recover damages for breach of warranty. Does this representation of the agent constitute a warranty? Why?

2. Howe bought a horse from a dealer who guaranteed him to be gentle and fit for any lady to drive. While Howe was trying the horse before the sale, the horse snapped at him twice, and became frightened at a train. May Howe later recover from the dealer on his warranty if it turns out that the horse is not gentle and fit for ladies to drive? Why?

3. Frank sold a carload of apples to Jeffreys, nothing being said at the time as to their quality. They were in the possession of Frank at the time they were sold and each party had ample opportunity to inspect them, but did not do so. It was later found that they were badly rotted, and Jeffreys sued for damages for breach of an implied warranty of quality. May he recover? Why?

4. Armour & Company's Wholesale Company sold a quantity of soap to Heyman & Company, retail merchants. They in turn sold a bar of this soap to Hasbrouck, who used the soap and because a needle which was imbedded in the soap scratched his hand, contracted blood poison and was ill for seven months. May he recover for breach of an implied warranty? If so, from whom, and for what?

5. Smith sold Brown an improved hayrack which he had made according to Brown's specifications for a particular purpose. Brown resold the hayrack to Jenkins, who resold it to Ordway. Subsequently Brown repurchased the hayrack of Ordway and then for the first time discovered that it was not at all suited for the purpose for which he had ordered it. He sued Smith at once for damages for breach of warranty. May he recover? Why?

## CHAPTER XXVIII

## REMEDIES OF PARTIES

**279. Remedies of Seller.** One who contracts to sell, or who sells goods, has certain well-defined remedies for wrongful acts of the buyer. These are of two kinds — primary and secondary remedies. The primary remedies are (1) recovery of the sale price, and (2) recovery of damages for wrongful refusal of the buyer to accept the goods. These primary remedies rest upon personal rights of the seller against the buyer and are enforced by means of a suit against him.

The secondary remedies of the seller rest upon rights, not against the buyer personally, but against the goods themselves. They are four in number, being (1) right of lien; (2) right of stoppage in transit; (3) right of resale, and (4) right of rescinding the contract.

**280. Recovery of the Price.** When the property in goods has been transferred to the buyer, the seller may recover the contract price. Similarly, if the buyer unreasonably refuses to receive goods covered by a contract of sale, when the seller tenders them to him, the seller may sue at once for the price.

#### EXAMPLES

1. Solomon contracted to buy of White a manikin for $35, $10 to be paid when the manikin was delivered at the express company's office and $5 every month thereafter until the whole was paid. White delivered the manikin to the express company, but Solomon refused to receive it. White sued and recovered the whole price, although the parties had stipulated in their contract that title should not be transferred until the whole price was paid. The seller had performed all his conditions and the wrongful total breach by the buyer gave rise to a right in the seller to recover the whole price at once. White vs. Solomon, 164 Mass. 516.

2. Putnam sold a pair of horses to Glidden and delivered them at Glidden's barn. Glidden refused to accept them, claiming a defect. Putnam sued Glidden for the price. Recovery of the price was allowed, Glidden failing to prove any defect. Putnam vs. Glidden, 159 Mass. 47.

**281. Recovery of Damages.** On a refusal by the buyer to perform his contract, the seller may elect to retain the goods and recover the money damages which he has suffered by reason of the buyer's refusal. The amount of these damages is the difference between the market value of the goods and the contract price. This difference represents the profit to which the seller was entitled by his contract. If the goods sold have no market price, the seller is entitled to the actual damages which he has suffered by reason of the refusal of the buyer to perform. This may in some instances be merely the outlay which the seller has made in preparing to perform; in others it may be the entire price of the goods.

EXAMPLE

Allen ordered from Funke twenty toilet sets, at a stated price, the order being in writing and accepted by Funke's salesman. Later Allen cancelled this order. Funke was allowed to recover the difference between the contract price and the market price of these goods. Funke vs. Allen, 54 Neb. 407.

**282. A seller's right of lien** is the right of the seller of goods to retain possession, even after title has been transferred to the buyer, as security for payment of the price. This right is lost if the goods are delivered to the buyer, and the seller's remedies are thereafter limited to the primary rights discussed in the two preceding sections. This right of lien is seldom exercised except when the seller suspects insolvency or bad faith on the part of the buyer.

EXAMPLE

Ames sells goods to Bates for $500 to be delivered one month hence, the goods being specified and in existence. The risk of loss and all other incidents of ownership are transferred at once to Bates, but Ames retains the right to keep the goods until the purchase price is paid. This is his right of lien.

**283. Stoppage in Transit.** Although the seller loses this lien the moment the goods pass from his possession, he is allowed to re-establish this lien and regain possession in some cases when the goods are in the hands of a common carrier for shipment to the buyer. If after shipment has been made the buyer becomes insolvent, the seller may regain possession of the goods by notifying the carrier not to deliver them to the buyer but to hold them for him. The right to do this is the right of stoppage in transit. If the notice is given before the carrier has delivered

the goods, the seller regains his right of lien, though he then must pay the transportation charges. If the goods are represented during transit by a negotiable receipt, the carrier is under no duty to redeliver the goods until this has been surrendered. The right of stoppage in transit is therefore lost when a negotiable receipt has passed into the hands of an innocent purchaser for value, for he thereby becomes the owner of the goods and entitled to possession on demand.

EXAMPLE

Eveleth sold logs to Ware and delivered them to a log booming and driving company to be floated down the Kennebec river to Ware's mills. While the logs were in the possession of the driving company, Ware became insolvent and transferred his property in the logs to Johnson, a trustee, to hold for Ware's creditors. Eveleth rightfully reclaimed the logs and retained them by his re-established lien for the purchase price. Johnson vs. Eveleth, 93 Me. 306.

**284. Right of Resale.** After the making of a contract of sale, if the buyer without cause fails, for an unreasonable length of time, to pay the price and accept the goods, the seller may resell the goods to another. In so doing he really acts as the agent of the buyer, in whom the title rests, and makes the resale merely to realize upon his lien for the unpaid purchase price. No notice of such resale need be given to the defaulting buyer. If upon the resale the amount realized is insufficient to compensate the seller for the original purchase price, he may then sue the original buyer for the difference, which will be the measure of his damages because of the buyer's wrongful refusal or neglect. It also is a logical conclusion that if the resale is for a greater sum than the original price, the excess belongs to the original buyer, though this case has never been presented to the courts.

EXAMPLE

Wrigley sold Cornelius 10,000 world's fair pictures at 15 cents each and delivered 6,000 of them. Cornelius refused to accept the balance and Wrigley sold them to another person for 10 cents each and sued Cornelius for the difference. He was allowed to recover this amount as damages for the wrongful refusal of Cornelius to perform the contract of sale. Wrigley vs. Cornelius, 162 Ill. 92.

**285. Rescinding the Sale.** Upon the refusal of the buyer to complete his contract, the seller may rescind the sale and keep

the goods as his own in satisfaction of his damage. If the value of the goods be less than the damage he has suffered, he may also sue for the excess. In cases where the buyer has committed a *fraud*, the seller may recover the goods even though they have been delivered to the buyer, for fraud makes transfers of property voidable.

EXAMPLE

Ackerman sold Rubens some goods, and while they were still in the possession of the seller, the purchase price being unpaid, the buyer notified Ackerman that he had changed his mind and did not wish the goods. Ackerman immediately sued for the difference between the contract price and the market value of the goods. This he was allowed to recover, retaining the goods as his own. Ackerman vs. Rubens, 167 N. Y. 750.

The following clear statement of the rights of the unpaid seller is made in the above case. "When the buyer of personal property, under an executory contract of sale, refuses to complete his purchase, the seller may keep the article for him and sue for the entire purchase price; or he may keep the property as his own and sue for the difference between the market value and the contract price, or he may sell the property for the highest sum he can get, and, after crediting the net amount received, sue for the balance of the purchase money."

**286. Remedies of the Buyer.** The remedies of the buyer for wrongful breach of the contract of sale by the seller are of two general types, depending upon whether or not title to the goods has been transferred. If the title has been transferred and the seller wrongfully refuses to carry out the terms of the contract, as by delivering possession, the buyer may either recover the goods or their money value. If title has not been transferred he can recover the amount of the damage which he has suffered by the breach of the seller, which is usually the difference between the contract price and the market price at the time of delivery, together with other expenses which the buyer has incurred in reliance upon the contract of sale.

EXAMPLES

1. Abraham contracted to purchase from Karger a quantity of goods stored in a warehouse subject to Karger's order, for the sum of $2500. Abraham later tendered to Karger this amount of money, but Karger refused to make delivery and offered to pay the difference between this sum and the market price of the goods. Instead of accepting this, Abraham brought an action, called replevin, to recover the particular goods as his own property, and this he was allowed to do, it being deemed that title had passed and that on the tender of the purchase price Karger was no longer entitled to retain even the possession of the goods for his lien. Abraham vs. Karger, 100 Wis. 387.

2. Walters contracted to buy of Simpson a certain lot of hardwood lumber, to be delivered in thirty days, at a specified price. Simpson instead sold this lumber to Jordan at an advanced price. Walters will be allowed to recover the difference between the price he agreed to pay and the market value of the goods, and the amount which Jordan paid will be evidence of this market value.

**287. Remedies for Breach of Warranty.** There has been much disagreement among the several states regarding the rights of a buyer for a breach of warranty by the seller. They have uniformly agreed that the buyer may always recover the damage which the breach of warranty has caused him, and some states have allowed the buyer to rescind the sale and return the goods as well. The uniform sales act, Section 69, adopts the latter of these views. It permits the buyer to refuse the goods if title has not been transferred, or if title has passed, to may rescind the contract, return the goods and sue for damages, upon the discovery of a breach of warranty. Or he may keep the goods and sue for damages resulting from the breach of warranty, which would be measured by the difference in value of the goods actually received and goods such as the seller represented them to be.

## REVIEW QUESTIONS

1. Bates shipped goods to Ames by railroad in compliance with an order, and took from the carrier a bill of lading to Ames, or order. He sent the bill of lading to Ames, who indorsed it and sold it to Call for value. Before the goods reached their destination Bates discovered that Ames was insolvent and sought to exercise the right of stoppage in transit. May he do this? Why?

2. Maxon sells goods to Williams, to be delivered in thirty days, the price to be paid at once. Williams fails to pay the price and Maxon notifies Williams that he intends to hold the goods for his lien. Thereafter and before the thirty days have elapsed, the goods are destroyed. Who bears the loss? Why? May Maxon recover the purchase price from Williams? Why?

3. A sells goods to B and delivers them to a carrier for shipment to B, receiving a straight bill of lading naming B as the consignee. B is insolvent at the time of the sale, but A remains ignorant of that fact until the goods have arrived at their place of destination. A orders the goods stopped when they are on the railroad's trucks ready to be taken to B's place of business. A then receives the goods and sells them at private sale without giving any notice to B. Has B any remedies? What? Why? Suppose that A received more for the goods than B had agreed to pay. Would this make any difference? Why?

4. Cox contracts to sell Adams 150 cases of shoes to be manufactured according to specifications furnished by Adams. When 50 cases have been completed, Adams notifies Cox that he does not want any of the shoes and will not accept them. Cox proceeds with the manufacture and completes the 150 cases and offers to deliver them, but Adams refuses to accept them. May Cox recover any damages? If so, what will be the measure of his damages? Why?

5. Ames, a dealer in Madison, orders furniture from Bates, a wholesaler in Grand Rapids. When the furniture arrives in Madison, Ames discovers that it is defective in several particulars and differs materially from the furniture described in the catalogue from which he ordered it. Bates refuses to take it back. Enumerate the rights of Ames.

# CHAPTER XXIX

## BAILMENTS

- I. For Benefit of Bailor
  - 1. Deposit
  - 2. Mandate
- II. For Benefit of Bailee
- III. For benefit of Both
  - 1. Pledge
  - 2. Hire
    - a. For use
    - b. For repairing, etc.
    - c. For care
    - d. For carriage
- IV. Exceptional Bailments (INVOLVE)
  - Inn-Keepers
  - Common Carriers

**288. Definition.** A bailment is a contract relation resulting from the delivery of personal property by the owner, called the bailor, in trust to a second person, called the bailee, for a specific purpose other than a sale, upon the accomplishment of which the property is to be dealt with according to the owner's direction.

In the study of bailments we shall therefore discuss the law relating to the borrowing, lending, hiring, the storing of goods for safe-keeping, the possession of goods by one doing work on them, and also their transportation by a common carrier or private carrier.

Any personal property may be the subject of a bailment. The delivery necessary to constitute one a bailee may be either actual, constructive, or by operation of law. The delivery of a watch to a jeweler for repair, of a horse to a smith to be shod, or of a package to an expressman to be carried, are familiar examples of actual delivery. The delivery of a key to a warehouse may be the constructive delivery of the goods therein. The holder of lost goods or of goods that have been seized under legal process is a bailee by operation of law.

**289. Importance.** When personal property is delivered by a bailor to a bailee, certain duties are created on the part of the bailee. Among these are the duty of returning the goods to the owner, or some other person designated by him, when the purpose of the bailment is satisfied; and the duty of preserving them during the existence of the bailment with varying degrees of care, depending upon the nature of the bailment. As goods are often in the hands of bailees — warehousemen, inn-keepers, common carriers, and the like — as a part of ordinary commercial transactions, the subject is of the utmost practical importance.

**290. Kinds of Bailment.** The subject of Bailment is divided into four general classes, based upon the nature or character of the relation between the bailor and the bailee. These, with their sub-divisions, are:

I. Bailment for the sole benefit of the bailor.
   (1) Deposit, when the property is to be kept by the bailee without charge, and is to be later returned to the bailor.
   (2) Mandate, or Commission, when the bailee is to perform work on the goods without charge, and to return them.

II. Bailment for the sole benefit of the bailee, as when property is loaned by the bailor to the bailee without compensation.

III. Bailment for the benefit of both bailor and bailee.
   (1) Pledge, or Pawn, when property is deposited as security for the payment of a debt, or the performance of some obligation.
   (2) Hiring, which may be (1) Hiring a thing to use; (2) hiring, or employing, work to be done on a thing; (3) hiring, or employing, one to care for a thing; and (4) hiring the carriage of a thing from place to place.

IV. Exceptional bailments involve:
   (a) Inn-keepers,
   (b) Common Carriers.

**291. Degrees of Care.** As soon as a bailee receives property, he should have a clear understanding of the degree of care

which is expected of him, so that he may know how to be held blameless if the property is lost or damaged. Because of the varying nature of the relation of the parties to a bailment, three degrees of required care have been established. These are:

| Kind of Bailment | Care Required | Degree of Negligence for which Bailee is Liable |
|---|---|---|
| For benefit of bailor | Slight | Gross |
| For benefit of bailee | Great | Slight |
| For mutual benefit | Ordinary | Ordinary |

By ordinary care is meant that degree of care which the average reasonable and prudent man in a similar situation would exert; by slight care, that degree of care that a man of common sense, however careless, absent-minded and inattentive, applies to his own affairs; and by great care, such care as one who had insured the property might exert, or that degree of care which a man remarkably exact and thoughtful gives his own property.

## BAILMENTS FOR BENEFIT OF BAILOR

**292. Deposit** is a delivery of goods to another to be kept and returned without recompense. A distinction is drawn between the ordinary deposit of money in a bank, subject to be withdrawn by check, and a deposit within this definition. The relation between the bank and the depositor is that of creditor and debtor, as the identical funds which are deposited are not to be returned, but merely an equivalent amount of money, upon demand. This is not a bailment.

### EXAMPLES

1. Smith took a package of bonds to a bank for safe-keeping, leaving them with the cashier. This was a special deposit, without compensation by either party, and Smith was entitled to demand and receive the return of the bonds at any time. Smith vs. First National Bank, 99 Mass. 605.

2. Stewart, a traveler, in passing through a city, stopped for a few hours, and not wishing to be burdened by his suit-case, left it with a clerk in a drug-store. The accommodation was given without expectation of pay, and was a deposit for the benefit of Stewart solely. Stewart vs. Head, 70 Ga. 449.

**293. Bailment for Mandate or Commission** is that class of bailment in which the bailee undertakes to do something for the bailor with reference to the thing bailed, without compensation. In deposit, the principal thing is the keeping, but in commission it is the work to be done. The word *commission*, in the sense in

which it is used here, is not like the commission or fee allowed to a broker on a sale of goods, but consists wholly in the doing (committing) of some act or service on the subject matter at the direction of the bailor, without reward for the service.

EXAMPLES

1. Taylor offered to carry money for Colyar to another town and to deliver it to Marlow, but finding it inconvenient to make the trip, gave the money to a neighbor, who undertook to carry it and deliver it as requested by Colyar. The neighbor, however, had his pocket picked while in a crowd. Colyar sued Taylor for the money and was allowed to recover, Taylor having been guilty of gross negligence in violating the terms of the bailment, and giving the money to another person to carry. Colyar vs. Taylor, 41 Tenn. 372.

2. Gill asked Middleton, a watchmaker, to examine his watch and make such repairs as were necessary. Middleton, out of friendship, offered to do this and to perform the necessary repairs without charge. Before Gill called for it, the watch was injured without fault of Middleton. The bailment was a commission, and Middleton was not liable for the damage caused Gill. Gill vs. Middleton, 105 Mass. 477.

**294. Rights and Duties of the Parties.** Formerly the two bailments of deposit and mandate were treated separately, but the same sort of custody and service are actually involved in the two types, and consequently the obligations of the parties to each other are subject substantially to the same rules. The only difference is one of emphasis. In deposits custody is the chief purpose, and the performance of an act is incidental. In mandates the service is primary, and custody is the incidental feature.

**Diligence.** In bailments for the benefit of the bailor, it is the duty of the bailee to take reasonable care of the goods. As he receives no benefit, the care required to free him from responsibility is slight, and he is liable only in the event that he be guilty of gross negligence. Reasonable care depends on the nature and value of the goods, and the circumstances of the particular transaction.

EXAMPLES

1. Foster deposited a cask of gold of the value of $50,000 with the Essex Bank for safe-keeping. This was stolen by the bank's cashier and chief clerk, together with a considerable amount of the assets of the bank. Foster sued the bank, but was denied recovery on the ground that the bank had used the same care to preserve his property as it had taken with its own money, and that this was a reasonable care under the circumstances. Foster vs. Essex Bank, 17 Mass. 479.

2. Knowles was notified by a railroad company that a shipment of hay had arrived for him. He acknowledged its receipt, paid the freight and asked that as a matter of accommodation it be left in the car for a few days. The car was side-tracked onto a wharf which two days later broke down because it was over-loaded and precipitated the hay in the river. When Knowles sued for damages he was denied recovery, it being decided that the railroad had ceased to be a common carrier as to him and was a mere depositary, and that it had not been guilty of gross negligence. Knowles vs. Atlantic etc. R. R. Co., 38 Me. 234.

Ordinarily such a bailee is responsible only when he does an act improperly or an improper act regarding the thing bailed, but is not liable for failing to do an act which an owner exercising great care of his own property might have performed.

EXAMPLES

1. Thorne asked the permission of Deas to leave a vessel at his wharf, and Deas volunteered to place insurance upon it, but failed to do this. The vessel was injured and Thorne sued Deas for his loss, but was denied recovery, as the bailment was a mandate, and Deas could not be held liable for failing to perform an act, though had he done an act with negligence he would have been liable. Thorne vs. Deas, 4 Johns. (N. Y.) 84.

2. A guest at a hotel requested the clerk to receipt and care for a registered letter which he was in expectation of receiving. The letter, containing $100, was delivered, receipted for and placed in the letter box of the hotel, from which it was stolen. It was shown that the hotel letter box was an unsafe place to leave letters, and the clerk and proprietor of the hotel were forced to pay the guest for the damage he had suffered, they having performed an act, which they undertook to do, and one which required special care, in a grossly negligent manner. Joslyn vs. King, 27 Neb. 38.

**Right to Use.** Any use of the article bailed by the bailee would change the deposit or mandate to the form of bailment for the mutual benefit of the parties. Only such use, therefore, as is incidental to the proper preservation of the thing, is allowed. If the bailee uses the thing other than in this manner, not only does the bailment become one of mutual benefit demanding a greater degree of care, but the bailee who wrongfully uses such an article becomes absolutely liable for any damage which may be done to it.

EXAMPLE

Preston deposited $12,000 in U. S. bonds with the bank conducted by Prather, for safe keeping. Subsequently, Preston secured a loan of a large

amount, leaving these bonds as security. The bonds were later stolen by Prather's cashier, whom Prather had every reason to believe was dishonest, he having a short time before been discovered in a gross irregularity in his books. It was admitted that Prather had not been guilty of gross negligence, but merely of a want of ordinary care. Preston was allowed to recover damages for the loss, the deposit having been changed to a bailment for mutual benefit, and as such a lack of ordinary care was sufficient to make Prather liable. Preston vs. Prather, 137 U. S. 604.

**Redelivery of Property.** In bailments for the benefit of the bailor, the bailee has nothing to gain by the continuance of the relation, and consequently the bailor may terminate it at any time and demand a return of his property. He must allow a reasonable time for redelivery and cannot put the bailee under any liability to incur any expense in making the return. The same privilege of terminating the relation belongs to the bailee. He must, however, like any other bailee, make redelivery to the right party at his peril. If he should deliver it to the wrong party he is liable for damages.

Ordinarily, readiness on the part of the bailee to return the property, in case of bailment for the benefit of the bailor, is sufficient.

A bailee has a lien upon the goods bailed, for the collection of reasonable or agreed expenses incurred by him in the keeping of the thing bailed.

EXAMPLE

1. Wear sued Gleason to recover the value of a trunk left at Gleason's hotel by one of Wear's traveling salesmen. It appeared that the salesman had asked permission to leave the trunk for his own convenience and that later Gleason had delivered the trunk to a third person, unknown to him, who called and requested its delivery, making no effort to find whether the claim to the property was based on any right. It developed that the third person was a thief. Wear was allowed to recover the value of the trunk and its contents from Gleason. Wear vs. Gleason, 52 Ark. 364.

2. A, for reasons of his own, desired B to see a valuable picture owned by C. He borrowed the picture of C and sent it by a son of B's, to B's house, where it was placed on a mantel, without the knowledge of B. The picture was injured by heat from the fire in the grate and C sued B for the damage to the picture. His right to recover damages was denied, although it was admitted that to place a picture in this place was gross negligence. This was because no one can be made to assume the responsibility of a bailee without his consent. Lethbridge vs. Phillips, 3 E. C. L. (Eng.) 523.

## REVIEW QUESTIONS

1. Bernard agreed as a matter of accommodation to remove some sugar and cider belonging to Coggs from one cellar to another. He removed the sugar, but set it down in a wet place, where it was ruined. He refused to move the cider at all, and Coggs was compelled to pay $30 to get this removed on account of the scarcity of labor. He now sues Bernard (1) for the value of the sugar, and (2) for the expenses in removing the cider. Could he recover?

2. Wilson entrusted a horse to Brett to ride to the town of Middleboro to show a prospective buyer. Instead of so doing Brett drove the horse to a race track beyond Middleboro, where as he was witnessing a race, the horse was run into and killed. Brett could not have avoided the collision. Could Wilson recover the value of the horse from Brett? Why?

3. Corcoran, a liveryman, agreed to take Chase's horse and train him to drive double with a horse which Chase was to purchase. Corcoran was to receive no compensation. He incurred expenses for horse-shoes while the horse was in his possession and refused to redeliver the horse until these expenses were paid by Chase. Chase, however, claimed that Corcoran was responsible for the expenses, as he derived a certain benefit from the use of the horse. Could Chase reclaim the horse without paying these expenses? Why?

4. Youl put certain goods on board Harbottle's packet boat running from London to Gravesend, Harbottle agreeing to carry them as an accommodation and to deliver them to Youl's agent at Gravesend. When the boat reached Gravesend a stranger came aboard, claimed to be Youl's agent and showed letters from Youl to him. Harbottle delivered the goods and it later developed that the stranger was an impostor who had found the letters. Youl sued Harbottle for the value of the goods. Could he recover? Why?

5. Manchester borrowed a horse to drive from Worcester to Clinton and return. On his return from Clinton he went out of his way on an errand to another city. Although he drove very carefully the horse stepped in a hole before he got back to Worcester, broke its leg, and had to be shot. Spooner, the owner of the horse, now sues to recover its value. May he do so? Why?

## CHAPTER XXX

## BAILMENT FOR BENEFIT OF BAILEE

**295. Gratuitous Loans** constitute the principal form of bailments made solely for the benefit of the bailee. In this sense the use of the word "loans" must be understood to refer to articles of personal property borrowed for use by the bailee, or borrower, without compensation to the bailor or lender.

**296. Rights and Duties of the Parties.** The borrower, though not liable for every possible injury which may befall the property while it is in his hands, is held responsible to use the highest possible degree of care which careful men use in the transaction of business, and in the conduct of their own affairs. Even slight negligence will render such a bailee liable to compensate the bailor in damages for his loss. This is because the relationship exists solely for the benefit of the bailee and while he cannot be deemed to insure the property he is required to guard it with the highest degree of care.

EXAMPLE

Green borrowed Hollingsworth's watch. He removed the chain, fastened a twine string and a key to it, put it in his pocket, and about three weeks later while on a hunting expedition lost the watch. Green was found to be liable as having been guilty of at least slight negligence. Green vs. Hollingsworth, 5 Dana (Ky.) 173.

**Use of the Thing Borrowed.** The borrower is confined strictly to the use for which the thing was loaned, whether this use was actually agreed upon or must have been implied from the nature of the article and the surrounding circumstances. A slight departure from the purpose of the bailment is at the peril of the bailee and makes him absolutely liable for any damage to the property.

EXAMPLE

A loaned a lathe to B for his personal use. B, having finished using it, loaned it to C, who without his fault damaged it. A immediately sued B for the damage and recovered, B by his wrongful act having become liable for anything which might befall the lathe. Fox vs. Young, 22 Mo. App. 386.

**Special Items of Liability of Borrower.** A borrower is required to pay all of the expenses necessarily arising from the use of the property. This is just, for he alone receives the benefit. Thus he is required to pay for the feeding, stabling, and shoeing of a borrowed horse. If he borrows machinery he must keep it in repair. On the other hand, he is not liable for extraordinary expenses, not incident upon the ordinary use of the article borrowed, and which arise without his fault.

EXAMPLE

Ames borrowed a valuable violin from Bates. Later the violin was stolen from Ames' house, during the absence of Ames, the doors having been securely locked. It also appeared that the thief entered through a window and stole a number of Ames' goods as well. Ames is not liable for the loss of the violin, he having used the greatest care.

**Liability of the Lender.** When a bailment is for the benefit of the borrower, the lender is liable for damage caused by defects in the article loaned if the damage is the result of an unsafe condition of the thing loaned, known to the lender and not communicated to the borrower, but not otherwise.

EXAMPLE

A had a defective steam boiler, which he loaned to B to use in certain work. B knew nothing of the condition of the boiler, and while in his possession it blew up without his fault and did considerable damage to his property. He was allowed to recover damages from A. Gagnon vs. Dana, 69 N. H. 264.

**Borrower's Right to Retain.** The borrower has the right to retain the article loaned for the period of the bailment, if specified, but upon its termination he must return it to the lender.

EXAMPLE

Lawson loaned Lay his team to take a load of corn to a neighboring market. On the way Lawson overtook Lay and demanded the return of his team. Lay had the right to refuse to redeliver the team until he had the corn at market. Lay vs. Lawson, 23 Ala. 377.

**Return of Property.** The bailee, or borrower, is under the duty of returning the property immediately at the end of the period for which the loan was made. He must also return all increase and profits of the borrowed property, except of course the benefits which come to him from the use of the property for

which it was loaned. The property must be returned to the bailor personally, and it is not sufficient merely to return it to his premises, unless his attention is specifically directed to the return. Nor does the borrower have any right of lien which entitles him to retain the property for the payment of a debt due him from the bailor. Neither can he retain the property by claiming that it did not belong to the bailor, for by his accepting the bailment he recognized the bailor's title and this he cannot later deny.

EXAMPLE

Esmay loaned his horses and carriage to Fanning to use, on an agreement that Fanning should return them to Esmay on demand. The property was in a livery stable belonging to Jones, where Fanning secured it, but later, having finished using it, he returned it to Esmay's private stable, in Esmay's absence, where it was destroyed the same night by fire. Esmay sued Fanning for the value of the property and was allowed damages. Esmay vs. Fanning, 9 Barb.(N. Y.) 176.

## BAILMENT FOR MUTUAL BENEFIT—PLEDGE

**297. A Pledge or Pawn** is a bailment to secure the performance of some obligation, with power of sale in case of non-performance. Every form of personal property may be the subject of a pledge. Evidences of ownership of property, such as bills of lading, warehouse receipts, negotiable instruments, stocks and bonds, as well as clothing, jewelry, and other forms of personal property may be deposited by the owner with another person to secure the performance of some obligation by the owner. This obligation often consists in the payment of a debt; in some instance, it consists in the performance of an act.

**298. Rights and Duties of the Parties.** Since this is a form of bailment for the benefit of both parties, the bailee is required to exercise ordinary care and is liable for ordinary negligence. He must guard the property, while it is in his possession, with the same degree of care with which the average, reasonably prudent man would guard his own property.

EXAMPLE

Jenkins pledged some stock at a bank as security for a loan of money. The stock was placed in the vault with the moneys and securities of the bank. Safe-blowers robbed the bank, taking Jenkins' stock, together with other valuables. The bank was not liable to Jenkins for this loss. Jenkins vs. National Bank, 58 Me. 570.

**Use of the Property.** As a general rule the pledgee, as the person who receives pledged property is called, does not have the right to use the property, except with the express permission of the bailor. His only right is to hold the property as security for the obligation for which it is given. The usual exception to this rule is in the case of animals which require moderate use to keep them in good condition and health.

EXAMPLE

Heath held stock belonging to Jones as security for a debt which Jones owed to him. Heath attempted to vote as a stock-holder of the company at an annual election. This he could not do, as he acquired no rights by virtue of the pledge, except the custody of the shares of stock as security for the payment of the debt. Heath vs. Silverthorn Company, 39 Wis. 147.

**Surrender to True Owner.** The bailee acquires no better rights than those of the bailor, and if the article pledged has been stolen, or found, or is wrongfully pledged by one not the owner, the bailee must surrender the property on demand by the true owner.

**Remedies of Bailee on Non-Performance of Obligation.** The bailee can retain the article pledged so long as the debt which it secures is unpaid. After the time has passed at which the obligation should have been performed, or the debt paid, the pledgee has certain additional rights. He may (1) sue the bailor and debtor upon the debt, without selling the pledge; (2) proceed in a court of equity to foreclose his lien against the property pledged, or (3) give reasonable notice to the bailor to pay the debt and redeem the property, and on his failure to do so may sell the property at an open and public sale, which must be free from all suspicion of fraud. An agreement in advance that the pledged goods can be sold at a certain time if payment is not made, is valid.

When the third remedy is used the bailee cannot himself be a purchaser of the article, nor can he sell it at a private sale, unless the conditions of the pledge particularly provide for it.

Until the bailee resorts to one of these remedies he continues to hold the property solely as security for the debt, and when the debt is paid, or payment is tendered, he must redeliver the

property in the same condition in which he received it. Should he return the property before the payment of the debt, he loses his right of lien and security.

As previously noted, the terms under which the sale may be made, including a waiver of notice, may be, and generally are agreed upon between the parties at the time the pledge is made. In the absence of such agreements the state statute governing the sales of pledged property must be allowed, and these statutes usually provide the time and manner in which notice of the sale must be given and also that the sale must be an advertised public sale.

If the pledged property be sold as provided in the agreement between the parties or as provided by statute, and the amount realized be insufficient to satisfy the debt, the bailor still owes the balance. If an amount greater than the debt be realized, the bailee must pay the excess to the bailor.

EXAMPLE

Marsh deposited ten cases of boots with Stearns to secure the payment of a note, which became due on November 8. On November 15, without notice to Marsh, Stearns sold the boots at public auction, realizing slightly less than the note, and sued Marsh for the balance of the note. Stearns was denied recovery and damages were allowed to Marsh, for the failure to give him notice to redeem was wrongful, and made the act of Stearns amount to an unlawful appropriation of Marsh's property. Stearns vs. Marsh, 4 Denio (N. Y.) 227.

## REVIEW QUESTIONS

1. Goodman pledged his life insurance policy with a bank to secure notes on which he owed money, and for sums to be borrowed from time to time at future dates. The notes were paid, Goodman died, and his executor demanded the return of the insurance policy, but the bank refused to deliver it, claiming that Goodman had borrowed other money which he had never paid. Assuming that the bank's claim is true, may the bank retain the policy?

2. Wilson bought a cargo of goods in London to be shipped to New York. Needing money to carry on his business, he took the negotiable bill of lading which he received to Little, a banker, and borrowed money on this security. He then sold the goods by means of a bill of sale to Johnson, who claimed the goods on their arrival in New York. Who would be entitled to receive them? Under what conditions?

3. Ames held property of Bates as security for a loan of $400. Being himself indebted to Call, he transferred the property of Bates to Call as

security or his debt to Call of $500. Ames demands the return of the property from Call, who refuses to give it up unless Ames will pay the $500 indebtedness. What are the rights of the parties?

4. Egan takes Dale's horse in order to try him before buying. Egan, not being able to drive himself, permits Fair, a competent horseman, to drive the horse. While being so driven, the horse is injured without the fault of either party. Who bears the loss? Why?

5. Murphy lends his horse to Simpson to drive. It is known to Murphy that the horse is a vicious animal and easily frightened by automobiles, but he does not inform Simpson of these characteristics. The horse runs away and injures both himself and Simpson. Who is liable in damages and for what?

## CHAPTER XXXI

## BAILMENT FOR MUTUAL BENEFIT — HIRE

**299. Hire** is a delivery of personal property to another to be used by him, or to be stored, transported, or worked upon by him, for a compensation. If the property is to be used by the bailee the compensation is to be paid by him to the bailor; but if the property is left with the bailee for some service to be performed on it, then the bailee receives compensation from the bailor. In either event the bailment is of the type of bailment for mutual benefit, for one party receives compensation and the other receives the use of it, or one party receives compensation and the other party receives the improvement, storage, or transportation of the thing bailed. Hire is treated under these two general sub-divisions: (1) Hire by the bailee; and (2) hire by the bailor.

**300. Hire by the Bailee** is a contract by which the bailee hires the use of the thing bailed, agreeing to pay to the bailor some compensation for its use.

**301. Rights and Duties of Parties.** The bailee for hire becomes entitled to the possession of the article for the period of the contract of bailment. The bailor must deliver the thing promptly and as agreed, and if it has become broken or is out of repair, the hirer may rightfully refuse to accept it. The bailor must not interfere with the hirer's possession during the period of the contract, and while he, being the owner, can sell his rights to a third person, he cannot sell the right to possession, for during the contract of bailment that right belongs to the hirer-bailee. The hirer is responsible for keeping the thing bailed in ordinary working condition, or for providing the ordinary food if the thing bailed is an animal, but the owner is responsible for extraordinary expenses necessary to preserve the property, occurring without the fault of either party.

EXAMPLE

French hired his horse to Devereux, and while in Devereux' possession the horse became ill without the fault of anyone. In order to save the life of the animal Devereux employed the nearest veterinary surgeon and on the recovery of the horse, the veterinarian sent his bill to French, who was compelled to pay the reasonable value of the services rendered. If the horse had become ill because of Devereux' fault he would have had to bear the expense. Leach vs. French, 69 Me. 389.

**Defects Known to Bailor.** The bailor is under the duty of informing the bailee of any known defects in the thing bailed which may injure the bailee. If he fails to do this he is responsible for any damage which may befall the bailee, who may rely upon the silence or statements of the bailor as to the condition of the thing bailed until he discovers the true facts to be otherwise.

EXAMPLE

Copeland, a mounted policeman, rented a horse of Draper, a liveryman who knew the horse was afflicted with a disease called "blind staggers," but failed to inform Copeland of this fact. While Copeland was riding the horse it staggered and threw him to the ground, breaking his leg and three ribs. Draper was compelled to pay Copeland for the injury sustained. Copeland vs. Draper, 157 Mass. 558.

**Right to Use.** The bailee-hirer must, in absolute good faith, use the thing hired only in the manner and for the purpose for which it was hired, or for purposes which may be fairly implied from the contract. If he should use the property for a different purpose, this would be a wrongful act, and he would be absolutely liable for any damage, regardless of the degree of care he used. Where one hires a horse to drive and uses it for heavy teaming, drives to a place other than that which he designated at the time he hired the horse, or otherwise materially and intentionally deviates from the purpose of the particular bailment, he is said to have dealt with the property as though it were his own, denying the rights of the owner. He is said to have "converted the thing to his own use." The result of such *conversion* is to make him liable for damage of any kind or nature which may befall the thing bailed before its return.

EXAMPLE

Wallace bought a barge load of coal of Cobb and hired Cobb's barge to transport the coal from Hawesville to Louisville, agreeing to return the barge immediately upon the conclusion of the trip. Instead of so doing Wallace used the barge on trips out of Louisville for two weeks. The barge was confiscated by persons in the military service of the United States. Wallace was responsible to Cobb for the value of the barge. Cobb vs. Wallace, 3 Cold. (Tenn.) 539.

**Degree of Care.** The degree of care required of the hirer while using the property within the purposes of the bailment is the same as in other bailments for mutual benefit. He is responsible for failure to use ordinary care. At the termination of the period of bailment he must return the property to the bailor in the same condition as it was when he received it, less the ordinary wear incident upon its reasonable use. He must also compensate the owner for its use according to the terms of the contract of bailment.

EXAMPLE

Hofer, having agreed to do certain hauling for Hodge, was unable to fulfill the agreement because of the illness of his teamster. He thereupon took the team to Hodge and told Hodge to employ a driver and have the hauling done, charging the expense to him. This Hodge did, but employed to drive the team an incompetent person, who backed them off a dock, the horses being drowned. Hodge was liable to Hofer for the value of the animals, as he had not used ordinary care in selecting a driver. Hofer vs. Hodge, 52 Mich. 372.

**302. Hire by the Bailor** includes the deposit of the bailed property with the bailee, under a contract of bailment by which the bailee agrees either to perform work on the thing bailed, to transport it, or to keep it safe for the bailor, for a compensation.

**Bailments for Performance of Services.** When the bailor delivers the property to the bailee, who agrees to perform work upon it for a compensation, the bailee is under the duty of exercising ordinary care both in keeping the article and in performing the services. This care must correspond with the care ordinarily exercised under like conditions.

EXAMPLES

1. Ames takes some fine gold ornaments and costly gems to a jeweler to be made into a necklace. The value of the articles and the character of the work required to be done make it essential that a highly skilled workman be employed upon it, and if the jeweler employs an apprentice who does the work in such a manner that the materials are injured, he assumes a liability for the damage to Ames.

2. Mrs. Lincoln took cloth to Miss Gay, a dressmaker, to be made into a dress. Miss Gay made up the dress with the goods wrong side out. Mrs. Lincoln was entitled to recover the value of the goods, for Miss Gay was bound to employ that degree of skill and care ordinarily possessed and used by dressmakers. Lincoln vs. Gay, 164 Mass. 537.

**Completion of Services.** The bailee must complete the work which he was employed to perform, before he can recover compensation. It sometimes happens that the thing bailed is destroyed while in his possession, preventing the completion of the work. If the article be destroyed without the fault of either party, the owner of the goods bears the loss and must also compensate the bailee for the work done at the time of destruction.

If the fault of the bailor prevents the completion of the services, the bailee may recover for the services rendered and for any loss naturally resulting from the bailor's wrong.

If, however, the bailee without cause abandons the work before completion, he cannot recover at all in many states, while others allow him to recover the value of the services actually performed less the amount of damage caused to the bailor by his refusal to complete the contract.

EXAMPLE

Ames delivers lumber to Bates, to be put into a building to be erected according to certain plans and specifications. Bates has performed half of the work when the building is destroyed by fire, without his fault. Bates is entitled to recover the value of the services already performed, and Ames must bear the loss of the building.

**Bailee's Right of Lien.** A workman employed to make up materials, or to alter or repair an article, has a lien upon it for his pay, and cannot be compelled to redeliver the article until he is compensated for his services. His lien gives him the right to retain possession of the article, but does not, except by special statutes in some few states, give him the right to sell the article

to secure his payment. This lien is terminated when the article is returned to the bailor, or to the bailor's agent, and cannot be re-established. It is likewise terminated by payment, or by the tender of payment, by the bailor, for the services performed. The lien for the entire charges of a single transaction may be enforced against such goods as remain in the bailee's possession, even though a part of the goods on which the charges accrued may have been delivered to the bailor.

EXAMPLES

1. Sensenbrenner delivered his buggy to Matthews to be provided with new iron tires. This work Matthews performed and then at Sensenbrenner's directions delivered the buggy to Maxwell, a painter, who had a shop in an adjoining part of the same building. Maxwell painted it and when it was completed Matthews took it back to his own shop where he claimed the right to retain it until he was paid for his services in tiring the buggy. This he had no right to do, having lost his lien by allowing the buggy to get out of his possession. He still had the right, however, to sue Sensenbrenner for the value of his services. Sensenbrenner vs. Matthews, 48 Wis. 250.

2. Minney mortgaged his boat to Scott, but retained possession, and ran it into Delahunt's dry-dock so that Delahunt might make repairs on it. Scott demanded the boat, but Delahunt was allowed to retain it until the charges for repairs had been paid. Scott vs. Delahunt, 65 N. Y. 128.

**Hire by Bailor for Safe-keeping.** An owner may leave his property with another for safe-keeping, compensating the keeper for his trouble. Warehousemen, grain elevator-men, bankers who maintain safety deposit vaults, agisters, and wharfingers are bailees for safe-keeping. An agister is one who takes in domestic animals to feed and keep, as a livery man who operates a boarding stable.

The duties of the bailees in such bailments are similar to those of bailees in any other form of bailment for mutual benefit. They are required to use ordinary care in guarding from injury the article bailed, to preserve and care for it according to the contract of bailment, and to return it to the owner at the termination of the period of bailment in the same condition as that in which they received it. They have a lien on the property for their charges for storage.

In the case of warehousemen a receipt is often issued, and if this receipt be negotiable in form, the rules regarding the transfer

of property by means of negotiable receipts, already discussed under the subject of Sales of Personal Property, apply.

Another bailee of this class is the commission merchant who has received goods to sell for the owner; he is required to keep them safely until they are sold.

EXAMPLES

1. Hensel left several horses and cows with Noble to pasture for him. He later attempted to remove one of the horses, but Noble refused to allow him to do so until the charges for pasturage were paid. Hensel proved that the other horses and cows were sufficient security for the payment of Noble's charges, but this proof did not entitle him to remove the horse, for an agister has a right of lien to all property in his possession until he is paid. Hensel vs. Noble, 95 Pa. St. 345.

2. Leidy placed poultry in a cold storage warehouse in good condition; but because the warehouse was kept too moist they became mouldy. The warehouseman was liable for the damage, as it was negligence to fail to keep the warehouse in fit condition for the storage of produce received. Leidy vs. I. C. Cold Storage Co., 180 Pa. St. 323.

**Hire by Bailor for Transportation.** The owner of goods may desire to have them transported from one place to another. For this purpose he employs some person to carry them, and this person becomes a bailee of the goods while they are in his custody.

Such persons are called carriers and may be either (1) private or (2) public carriers. The duties of public carriers are discussed in the next chapter on Exceptional Bailments.

A private carrier is one who occasionally carries goods of another, but who does not hold himself out as a carrier of goods for the general public. He differs from the common carrier in that he has the full right to contract when and with whom he pleases, without any special regulations or duties imposed by statute. Private teaming contractors, draymen, messengers, and occasional carriers by boat, wagon, or other vehicle, come within this classification. Since they are carriers for hire their only duties are to exercise ordinary care for the preservation of the goods, to perform the services agreed upon, and to deliver the goods on payment of their charges.

EXAMPLE

Sackrider at the request of Allen carried a load of grain on his boat at an agreed price between two river towns. Sackrider was not regularly engaged in this business. During the journey the grain was destroyed during a storm. It was admitted that Sackrider had exercised ordinary care. If Sackrider had been a common carrier he would have been liable, but Allen was denied recovery because Sackrider was a private carrier and had used ordinary care. Allen vs. Sackrider, 37 N. Y. 341.

## REVIEW QUESTIONS

1. McDuffie hired a horse and buggy to drive to Durham, but drove it to Hampton, two miles from Durham. Without any fault of McDuffie, the horse was run into at Hampton and killed. Wentworth, who owned the horse and had hired it to McDuffie, sued for its value. Could he recover? Why?

2. An officer of the American District Telegraph Company hired from Walker a team and surrey for the company's business. Having completed their use he sent them back in care of a small boy, who stated he was experienced with horses. The boy was not familiar with horses, however, and the team ran away, one of the horses being injured so that it had to be shot. Can Walker recover of the American District Telegraph Company for his loss?

3. Ames stored his goods in Bates' warehouse. While making repairs upon the timbers and beams of the warehouse, Bates removed some of the goods, but allowed Ames' to remain. During the process of repair, which was being done by competent workmen, the building collapsed and Ames' goods were damaged. Ames sued Bates for the amount of loss. Could he recover? Why?

4. Cox placed a box of dry goods on a dock belonging to O'Reilly to be carried on one of O'Reilly's boats, but neglected to give any notice to O'Reilly of the delivery of the goods. The goods were lost and Cox sued O'Reilly for their value. Can he recover?

5. Schmidt stored 99 tons of hemp with Blood, a warehouseman. At various times he received all but six tons, which Blood refused to deliver until all the charges for storage on the entire lot of hemp had been paid. Schmidt sued to recover the six tons, claiming that Blood had lost any lien which he might have had by allowing a part of the hemp to leave his possession. He also offered to pay Blood the storage charges on six tons of hemp. May he recover it? Why?

## CHAPTER XXXII

## EXCEPTIONAL BAILMENTS

**303. Introduction.** There are two types of bailees regarding whom the ordinary rules concerning the bailee's rights and duties in respect to the thing bailed do not apply. These are (1) inn-keepers, and (2) common carriers. The exceptional rules applying to these two classes of bailees also apply in general to the operations of telegraph and telephone companies though neither are bailees in the strict sense of the term.

**An Inn-keeper** is one who offers to accommodate all comers with the conveniences usually supplied to travelers. One is not an inn-keeper when he provides occasional entertainment only; nor is one who keeps a restaurant and provides food only. Neither is the keeper of a lodging house who makes separate contracts with each guest and reserves the right to refuse entertainment arbitrarily; nor are sleeping car companies considered to be inn-keepers. A steamboat company may or may not be an inn-keeper, depending entirely upon all the circumstances of its business.

**Who are Guests.** Those who take accommodations at an inn as transients, not including those who make the inn their permanent home, are rated as guests. This is true even though they be given special rates, as is frequently done with commmercial travelers, ball players, or other frequent patrons.

**304. Rights and Duties of Inn-Keepers.** The inn-keeper having taken upon himself a public employment must serve the public. His first duty is to receive to his inn as guests without discrimination such travelers as may ask for entertainment. He cannot select his guests. This is a duty imposed by law, and if when he has adequate accommodations, an inn-keeper refuses without cause to receive a guest, he is liable to compensate the person refused, in damages. An inn-keeper may, however, justify a refusal by showing that his accommodations were

already exhausted or that the person refused was without funds to pay for the accommodations; was disreputable, drunken, or disorderly; was affected with a contagious disease; or resorted to the inn for an illegal purpose.

As soon as a person becomes a guest, the inn-keeper under the common law practically insures his safety and the safety of his personal property of the kind which travelers usually carry with them. This liability does not depend at all upon whether the inn-keeper has used care to prevent the loss, or injury, but he is liable regardless of his own carefulness. The only exceptions to such liability, under the common law, are when the loss or injury is caused (1) by an inevitable accident, as a flood, called an act of God, (2) by the act of a public enemy, or (3) by the negligence of the guest.

These rules have been somewhat relaxed by statute in the several states, though there is no uniformity in this regard. It is, however, now quite generally established that the inn-keeper is freed from responsibility for damage occasioned by accidental fire, not due to his fault, or by other similar accidents. He is also allowed to limit his liability by special contract with the guest to that of an ordinary bailee for hire. For example, by giving notice to the guest that he will be responsible for valuables only when deposited in his safe, the inn-keeper may limit his liability in that regard. He cannot, however, escape liability for damage or loss to wearing apparel, or articles usually worn on one's person. Some statutes limit the total amount of an inn-keeper's liability to any one guest.

The inn-keeper has a lien on the property of a guest for the payment of the bill of the guest.

EXAMPLE

Caswell, a traveling salesman for DeWald & Co., left a valise containing $235 in the cloak room of a hotel, from which it was stolen. The hotel had no checking room, nor safe for the keeping of valuables. Recovery was allowed against the hotel, even though the clerk had not been notified of the contents of the valise, and regardless of the fact that it was not shown that the hotel keeper had been guilty of a want of ordinary care. Bowell vs. DeWald & Co., 2 Ind. App. 303.

**305. A Common Carrier** is one who regularly undertakes for hire to transport goods or passengers between different places, for such as may choose to employ him. To be a common carrier one must (1) carry on a public employment and (2) his business must be one of carriage for hire. As a consequence of his occupation he is then required (1) to carry any goods which may be offered of the kind he professes to carry, (2) by the means and over the route he has established; and upon his refusal to carry such goods must compensate the person refused in damages. For convenience the carriers of goods and of passengers are treated separately.

**306. Rights and Duties of Carrier of Goods.** *To Accept Goods.* The common carrier, being engaged in a public undertaking, is obliged to accept for carriage all goods offered him for transportation which come within the limits of the classes of goods he represents himself as carrying. A freight-carrying road cannot be compelled to carry money, nor an express company grain in bulk, or iron ore, which are properly carried by companies with suitably constructed cars. But the carrier cannot discriminate between persons, and must render the same services alike to all who request them. The carrier must exert reasonable dispatch, and must take notice if the goods are specially marked, as "Glass," "Perishable," and use suitable care to prevent loss or injury. Transportation may be refused, however, on the ground that the facilities are inadequate, or on account of special conditions outside of the carrier's control.

EXAMPLES

1. Rae offers grain to a railroad company to carry from Rockford to Chicago. The company at first refused to furnish cars, though it finally did so, but after providing them, delayed the shipment. Rae sued for damages and recovered the difference between the market price of the grain when it was finally delivered and the market price when it should have been delivered if it had been shipped promptly upon receipt. G. & C. U. R. R. Co. vs. Rae, 18 Ill. 468.

2. The Milwaukee Malt Extract Company offered a railroad a consignment of boxes labeled "beer," directed to a city in Iowa, which state had a statute forbidding the sale or delivery of liquor within the state, and providing a penalty for its violation. The railroad refused to accept the shipments

on this ground. The shipper sued for damages but could recover nothing. The refusal was rightful. Milwaukee Malt Ext. Co. vs. Railroad Company, 73 Iowa 98.

3. Shanley offered a railroad company a package for carriage. The package was unlabeled and contained nitroglycerin. The railroad refused to carry it unless labeled. This Shanley refused to do and sued the railroad for damages. He was allowed no recovery, the demand of the carrier being reasonable and for the protection of other property. B. & M. R. R. Co. vs. Shanley, 107 Mass. 568.

*Right to Compensation.—Rates.* The primary right of the carrier is to be paid for the services rendered, and like other bailees for mutual benefit he has a lien on the goods while in his possession for the payment of his charges. Except as controlled by statute the rate of compensation is fixed by the contract of bailment and carriage, though it cannot be more than a reasonable rate. It is, however, the right of the state to regulate rates to be charged by common carriers, providing a reasonable rate, and this has been done quite generally. The Federal government also can regulate the rates to be charged on interstate shipments. The Interstate Commerce Commission, created by Congress in 1887, has the power to establish and fix uniform rates, to investigate complaints, and regulate common carriers generally. Rebates have been prohibited and discriminations between shippers have been declared unlawful by statute. The purpose of these statutes has been to prevent a common carrier from favoring a shipper, or a class of shippers, at the expense of some other person or class.

EXAMPLES

1. Wilson sued a railroad company for $2700 as excess freight on a shipment of lumber. Freight was charged according to a public circular, but Wilson claimed that there had been an oral agreement for a lower rate. The goods were represented by a bill of lading which stated that the regular rates should apply. Wilson was denied recovery, it being impossible to modify a written contract by oral evidence. Louisville etc. R. R. Co. vs. Wilson, 119 Ind. 352.

2. Cook shipped goods by a railroad and paid the rate of $60 a carload. He later discovered that the railroad, while requiring a similar rate from other shippers of like commodities, had rebated them parts of this amount of from $3 to $20 a car. He then sued for $2700, representing the excess which he had paid over that of preferred shippers for a number of years, and was allowed recovery, the duty of a common carrier being to render service impartially. Cook vs. C. R. I. & P. Ry. Co., 81 Ia. 551.

**Liability for Loss and Damage.** The liability of a common carrier of goods is an exceptional one, being that of an absolute insurer of the safety of the property while in its custody and control. If the property is lost or injured the law presumes that the carrier was negligent and he can escape liability only by showing that the loss was occasioned by (1) Act of God; (2) Act of public enemy; (3) Act of the Shipper; (4) Nature of the Goods; or (5) Act of Law.

With these exceptions, the liability of a common carrier for the safe delivery of the goods is one of the most stringent and severe liabilities known to law. These exceptions are briefly defined as follows:

**An Act of God** is some unusual force of nature, without the interposition of any human agency, which the shipper could not anticipate. Thus lightning, tempest, cyclones, or floods will excuse the carrier from liability for loss. Because of its extraordinary character the Johnstown flood in Pennsylvania in 1889 was an act of God which relieved the railroads from liability. Ordinary spring freshets which occur annually and which might easily be guarded against do not excuse the carrier.

**An Act of a Public Enemy** is an act of the enemies with whom the country is at war. The acts of mobs, rioters, robbers, strikers, and insurgents will not relieve the common carrier from liability.

**An Act of the Shipper** may relieve the carrier of liability for loss, in case the act is negligent and is one of the principal causes of the resulting loss. Thus the misdirecting of goods by a shipper or the concealing of value of goods when asked as to value thereby preventing the carrier from knowing how to safely guard the shipment, are acts which may contribute to the loss, and relieve the common carrier of liability.

**The Nature of the Goods** may sometimes cause the loss and when this is the case the carrier is not liable. Thus it is the nature of fruit to ripen and rot, and of animals to trample upon each other, and when the loss is caused in this manner, the common carrier is not liable without proof of other negligence.

**Acts of the Law** may also relieve the carrier, as when goods are seized and confiscated by a public officer and destroyed by him as injurious to the public health or for some other cause, or when goods are seized under a levy and execution against the owner.

EXAMPLES

1. Kinnick shipped a carload of hogs by a common carrier. The hogs crowded about the car door for air at each stop of the train and several were killed. Kinnick was entitled to no recovery. Kinnick vs. C. M. & St. P. Ry., 69 Ia. 665.

2. A flood caused by a cloud-burst destroyed Wald's property in the possession of a common carrier. The carrier was not responsible to Wald for the loss. Wald vs. Railroad Company, 162 Ill. 545.

3. Pingree shipped goods by a carrier to Belden, and while *en route* the goods were seized by a sheriff on a levy and execution against Pingree. This levy was later declared invalid and illegal by the court and Pingree then sued the carrier for allowing the sheriff to seize the goods. He could not recover against the carrier, who was not bound to defend against an officer of the law with papers which purported to be regular. Pingree's proper remedy was against the sheriff. Pingree vs. D. L. & N. R. R. Co., 66 Mich. 143.

4. Hart shipped goods, horses and provisions by a carrier and placed his servant, Black, in the car to care for the animals and property. While Black was asleep, his lantern set fire to the goods, which were destroyed. Hart then sued the railroad for his loss. He was denied recovery. Hart vs. C. & N. W. R. R. Co., 69 Ia. 485.

**Limiting Liability.** Limitations of liability for loss or damage to goods, when contained in the bill of lading under which the goods are shipped, are binding on shippers unless contrary to law or public policy. The carrier cannot, however, limit its liability for at least ordinary care. In 1916 Congress enacted a law making all limitations of liability in bills of lading respecting interstate shipments unlawful, unless the limitations were first approved by the Interstate Commerce Commission. It also provided that no such approval should be granted in respect to ordinary live stock.

**Termination of Liability.** The liability of the common carrier ends when the goods have been delivered to the person to whom they are consigned. The carrier is responsible for wrongful delivery to unauthorized persons.

When the goods are at the end of their journey and are held for the order of the consignee by the railroad as a mere custodian, the extraordinary liability of a common carrier terminates, and the railroad is then liable only for ordinary care as a warehouseman. The Massachusetts rule, followed in Illinois, Indiana, Missouri, and Iowa, is that when the goods are stored at the end of their journey the railroad is merely a warehouseman. The New Hampshire rule, followed in Vermont and Wisconsin, is that the liability as a common carrier continues until the consignee has actually received the goods, or has had an opportunity of inspecting them and removing them in the ordinary course of business. The Michigan rule, followed in New York, is that the liability as a common carrier continues until the consignee has been notified of the arrival of the goods and has had a reasonable opportunity to remove them. The Michigan rule is favored in the majority of other states. It therefore is important for the carrier to notify the consignee on the arrival of the goods and for the consignee to remove them within a reasonable time.

Hasse shipped goods "C. O. D." to three parties, and on the arrival of the goods, two of the parties were notified, but the third could not be found. The parties notified asked permission to leave the goods for a week. Hasse was notified of all these facts and telegraphed to hold all the goods at the destination until they were paid for. Two days later the railroad warehouse was destroyed by fire without the fault of the company. Hasse sued for the value of the goods, but was denied recovery, the liability of the common carrier having been changed to that of a warehouseman. Hasse vs. American Express Co., 94 Mich. 133.

**307. Common Carriers of Passengers.** Passengers are not "goods" or personal property, and the common carrier of passengers is not a bailee in the strict sense, but his liability is very similar to that of a bailee and is therefore considered in this chapter.

Any one who is being transported in the vehicle of a carrier for hire from place to place, or who is at a station of a carrier with the intention of entering as soon as possible the vehicle provided, is a *passenger*. It is not essential that he shall have paid his fare, though he must be ready to do so upon demand, either in cash or by ticket.

*Liability of Carrier.* The liability of a common carrier to passengers is quite different from his liability for shipments of goods, for he is only responsible for injuries resulting from negligence. He is in no sense an insurer, though he must exercise a high degree of care in providing suitable and safe means of transportation, commensurate with the class of service which he represents himself as furnishing. The approaches to vehicles, platforms and stations must be kept in a safe condition, and protection must be furnished against insult, violence, and theft. The common carrier is responsible for the conduct of his servants. He must serve all comers without discrimination.

EXAMPLES

1. After Mrs. Brown purchases a ticket from the N. & O. R. R. Co., and while she is checking her baggage at the station, she is injured by persons scuffling. She can recover damages for her injury, as the company owed her the duty of providing safe facilities for the transacting of business incidental to her journey.

2. Putnam was riding on a street car, and becoming annoyed at the actions of an intoxicated man, requested the conductor to quiet him. This the conductor did by taking him to the front platform, where he was quiet until the car stopped, when the intoxicated man seized the car-hook, re-entered the car and killed Putnam. The street car company was not responsible for this death, the conductor having no reason to believe that there was any danger after he quieted the intoxicated man, and having used sufficient care. Putnam vs. Broadway etc. Railroad, 55 N. Y. 108.

3. Magoffin, a railway mail clerk, while on a mail car performing his duties, was killed by a collision between two of the carrier's trains. He had paid no fare, but was riding by reason of a contract between the government and the carrier. As such he was a passenger, and the collision being due to the negligence of some of the railroad employees, the carrier was held liable. Magoffin vs. M. P. Ry. Co., 102 Mo. 540.

**Rights of Carriers.** In order to protect his interests and to properly conduct his business, a carrier may make reasonable rules and regulations for the operation of his vehicles and conduct of the passengers, and may insist upon being paid in advance.

The carrier's liability ends as soon as the passenger has left the vehicle and has had a reasonable time to leave the platform or station of the carrier.

Conditions printed on tickets bind the passenger only if they are reasonable and not contrary to public policy. Whether the liability for negligence may be limited by contract is a disputed question. Such limitation is allowed in England and New York, but the United States Supreme Court and most state courts regard such contracts as violations of public policy, although it is generally permitted for the carrier to limit his liability to a passenger carried without charge.

EXAMPLES

1. Parry bought a reduced rate excursion ticket, which stated that it was good for transportation only on certain trains. To save time on the return trip he boarded an earlier train, the conductor of which refused his ticket, and on Parry's refusal to pay the regular fare ejected him. Parry sued, but was denied recovery of damages as the right of the carrier to limit the ticket by special contract in this manner was a reasonable one. Penn. R. R. Co. vs. Parry, 55 N. J. L. 551.

2. Warner had been a passenger on a train and was told to alight at a place some distance from the station. He was required to cross tracks and in doing so stepped into a hole in the planking and was injured. He was awarded damages for his injury, the railroad still being liable to him as a passenger. Warner vs. Railway Co., 168 U. S. 339.

**Baggage.** A passenger is entitled to carry with him such personal effects as are necessary for his journey. The carrier may limit the amount which will be carried free, and is responsible as an insurer only for personal baggage unless he accepts other articles as baggage with full knowledge of their character.

**308. Telegraph and Telephone Companies** are treated as common carriers by the courts of many states, on the theory that they are the carriers of intelligence, or news. They are generally held liable for the highest degree of care, and are required to serve all who apply without discrimination, like all common carriers. They are liable for the non-delivery of messages, for erroneous transmission, and for failure to maintain efficient and proper means of communication in accordance with their representations to the public. Their rates are subject to public regulation.

**309. The Post Office Department,** or that branch of the government which carries mails, performs functions similar to

a bailee for hire. It is a public, or common, rather than a private carrier. But while its operations are in their nature like those of common carriers, yet the government incurs no liability, since the sovereign state cannot be sued except by its own consent and consequently the courts cannot lay down rules of liability. The liability of the post office department is determined by its own rules and regulations.

## REVIEW QUESTIONS

1. Sibley left his horse over night in the stable of Aldrich's inn, where he was a guest. The horse was kicked by the horse of another traveler, and his leg broken. Aldrich proved that this was due to no fault of his. Could Sibley recover for the damage? Why?

2. Hinkle sued to recover damages due to delay in shipment of a carload of cattle. The cattle were injured, had to be fed *en route*, and missed the Saturday market. The contract on the bill of lading provided that the railroad should not be liable for injuries not caused by the gross negligence or fraud of its employees. It was admitted that the delay was caused by carelessness of a train dispatcher which did not, however, amount to gross negligence. Could Hinkle recover? Why?

3. Springer, the employee of a tenant in a building, was injured while riding in the public elevator maintained by the proprietor of the building, negligently operated. He sued the proprietor of the building for his injury. Could he recover? Why?

4. Udell had received a transfer from one branch of a car-line to another, and was required to cross a track to take the second car. While so doing, he was struck by a trolley pole, which broke while being changed from one end of the car to another. This was the pole on the car which he had left. Udell sued for damages for his injury. Could he recover? Why?

# CHAPTER XXXIII

## AGENCY

- I. Kinds
  - 1. General
  - 2. Special
- II. Manner of Appointment
  - 1. Express agreement
  - 2. Implied agreement
- III. Duties of Agent
  - 1. To Principal
    - a. Loyalty to trust
    - b. Duty to account
    - c. Duty to use skill
  - 2. To third persons
    - a. Acts in excess of authority
    - b. Acts for undisclosed principal
- IV. Duties of Principal
  - 1. To agent
    - a. Payment of compensation
    - b. Protection against loss and injury
  - 2. To third persons
    - a. As a disclosed principal
    - b. As an undisclosed principal
- V. Duties of Third Persons
  - 1. To agent
    - a. On contracts
    - b. For wrongful acts
  - 2. To principal
    - a. On contrcts
    - b. For wrongful acts
- VI. Dissolution
  - 1. By original contract
  - 2. By act of parties
  - 3. By operation of law

**310. Agency** is that relation founded upon the express or implied contract of two parties, by virtue of which one party is employed and authorized to represent and act for the other in dealings with third persons. The one who is thus authorized to act is called the *agent*, and the one for whom he acts is called the *principal*.

Agency is the result of a contract between the parties, and can usually exist only with the assent of the principal. The law implies the right of one person to act as agent for another in a few limited instances. These are: (1) the right of the wife to buy necessaries on her husband's credit, in which case she acts as her husband's agent; (2) the similar authority of an infant child to buy necessities, in certain cases, upon the father's credit; and (3) the authority of the seller of personal property in certain cases to sell the goods still in his possession to secure his pay. With these exceptions, in which the authority is created by law, the authority of an agent must be created by a contract, express or implied, between the principal and the agent.

**311. Comparison with a Servant.** The relation of principal and agent bears a close resemblance to that of master and servant, but is not identical with it. The characteristic of an agent is that he is a business agent and is clothed with discretion in matters of his employment, having the power to bind his principal in contracts with third persons when such contracts are within the scope of his authority. The function of the servant is to execute the commands of his master, usually upon or about things, without any power to represent his master in business dealings with others.

EXAMPLE

If A says to B, "Go into the market and buy me a horse," A's purpose is that B shall go out and find a person who has a horse for sale and make a contract with that person to sell the horse to A. B is then acting as an agent. If, when he brings the horse to A, A says to him, "Put the horse in the stable and care for him," and B does so, he is then a servant.

**312. General and Special Agency.** If agents be classed according to their authority to act for their principals, they may be treated as (1) general, and (2) special. A *general* agent is one having general authority to act in reference to some trans-

action or to some kind or series of transactions. A *special* agent is one authorized to act only in a particular event and in accordance with specific instructions.

EXAMPLES

1. A was appointed agent for the state of Illinois by B, an insurance corporation, to appoint sub-agents, accept risks, and collect premiums. This made him a general agent. Fishbaugh vs. Spunangle, 118 Iowa 337.

2. A was engaged by B to purchase a trotting horse, to match one already owned by B in age, size, color, and price. This made him a special agent. Davis vs. Talbot, 137 Ind. 235.

Since the powers of the special agent are limited, third persons dealing with him must find out just how far he has authority to bind his principal; otherwise they deal with him at their own risk.

The powers of a general agent are much broader, being unrestricted within the specified field, except by generally recognized customs, or by necessity. If the principal secretly limits the powers of his agent, and deceives a third person, he cannot escape liability by such secret limitation. The general agent is considered to possess the power to bind his principal, implied by the customs in his line of business, and possesses a wide discretion in the manner of performing his duties.

EXAMPLES

1. Ames is made a special agent to sell a farm for Bates, who owns several farms. Call deals with Ames, who tries to convey land other than the particular piece which he has been authorized to sell. Call cannot hold Bates on a contract made in this manner, as he failed to ascertain the nature and extent of the powers of Ames, who is a special agent. Ormsby vs. Graham, 123 Iowa, 202; Winders vs. Hill, 141 N. C. 694.

2. Ames was made sales agent for Bates in certain towns and counties in Illinois and represented himself as a general agent. Call bought goods from Ames, on terms of payment and at a price not authorized by Bates. The contract would, however, be binding upon Bates, as Call would have the right to rely upon the apparent authority given to Ames, and those ordinarily possessed by agents of that class. Walsh vs. Hartford Fire Insurance Co., 9 Hun. (N. Y.) 421.

**313. Purposes for Which Agency May Be Created.** It is the general rule that an agency may be created for the transaction of any lawful business, and that whatever a person may lawfully do, if acting in his own right, and in his own behalf, he may lawfully delegate to an agent.

**314. Who May Be an Agent.** Any person who is competent to contract generally, is competent to act as an agent. The rule goes further and renders competent to act as agents many persons who could not contract for themselves, such as infants, married women, and corporations. The reason for this is that many persons are competent to execute for others, what they would be incompetent to plan or direct. If the principal is willing to risk his business in the hands of one who is incompetent, he cannot later complain of the legal or mental disabilities of the agent, as against innocent third persons.

EXAMPLE

Nelson sent his minor son, Amos, to collect money due to him and to pay his bills. He was later sued for a contract made by Amos for him incidental to this work. He was liable on this contract, although Amos could not have validly contracted in his own behalf. Stanley vs. Nelson, 28 Ala. 514.

**315. Manner of Appointment of Agents.** Except in those cases in which the law creates the authority, the agent can only be appointed at the will and by the act of the principal, although that will may find expression in many different ways. The authority of an agent to bind his principal rests upon an agreement. This agreement may be (1) express, or (2) implied. In general, it need not be in writing, but there are exceptions in some states.* The formal method of appointing an agent is by means of a legal instrument called a "Power of Attorney." (This means "Power or authority to act as my agent.") Such instruments are required in some states in order to give authority to execute conveyances of real estate, and are usually required to be recorded with the proper county officer in a manner similar to the recording of the deed, or mortgage. When they are to be recorded, such Powers of Attorney must be executed in the same manner as are conveyances of real estate; for instance, they must be acknowledged before a notary public, with witnesses, in states requiring such formalities.

* In some states, to sell, mortgage, or lease lands, an agent must have a written authority. Alabama, California, Colorado, Illinois, Michigan, Missouri, Pennsylvania, and Ohio.

POWER OF ATTORNEY

**Know All Men by These Presents,** *That I, the undersigned, J. H. Cox, of the city of Galesburg, County of Knox and State of Illinois, have this day made, constituted and appointed, and do by these presents make, constitute and appoint Wm. Bachrach, of the City of Chicago, in the County of Cook and State of Illinois, my true and lawful attorney, for me and in my name, to sell and dispose of, absolutely, in fee simple, the following described lot, tract, or parcel of land, or any part thereof, situate, lying and being in the County of Cook, and State aforesaid, to wit: Lot* 10, of *Block* 8, *in Cooper's Addition to the city of Evanston, according to the recorded plat thereof, for such price or sum of money, and to such person or persons as he shall think fit and convenient; and also for me and in my name, and as my act and deed, to sign, execute, acknowledge and deliver such deed or deeds, and conveyance or conveyances, for the absolute sale and disposal thereof, or of any part thereof, with such clause or clauses, covenant or covenants, and agreement or agreements, to be therein contained, as my said attorney may think fit and expedient; hereby ratifying and confirming all such deeds, conveyances, bargains, and sales which shall at any time hereafter be made by said attorney touching or concerning the premises.*

**In Testimony Whereof,** *I have hereunto set my hand and seal, on this tenth day of August, A. D.* 1915.

*J. H. COX.* [Seal]

In the Presence of:
*GEORGE JONES,*
*THOMAS MURPHY.*

County of Knox } ss.
State of Illinois }

*On this* 10*th day of August, A. D.* 1915, *personally appeared before me the above named J. H. Cox, known to me to be the person who signed the foregoing power of attorney, and acknowledged that he signed the same as of his own free will and act and for the purposes therein mentioned.*

[Notary's Seal] *GEORGE SMYTHE,*
*Notary Public, Knox County, State of Illinois.*

Whenever a person has held out another as his agent, authorized to act for him in a given capacity; or has knowingly and without dissent permitted such other to act as his agent in that capacity; or when his habits and course of dealing have been such as reasonably to warrant the presumption that such other was his agent, with power to act for him, he cannot later deny the existence of the agency. In these instances, the contract of agency is implied from the surrounding circumstances.

EXAMPLES

1. Mrs. Horton, the owner of some personal property in a distant city, requested Jordan, residing there, to obtain offers on the goods. Jordan communicated a number of offers to Mrs. Horton, who finally sold the goods on her own account. About the same time Jordan also sold the goods, and a suit was started between the purchasers from Mrs. Horton and from Jordan. It was decided that Jordan had no authority to sell, and that the circumstances were not such as to lead others to believe that he did. The purchaser from Mrs. Horton was given the goods. Graves vs. Horton, 38 Minn. 66.

2. Hubbard sued Tenbrook for goods sold to Sides, as the agent of Tenbrook. It was proved that Sides had been conducting a grocery store in his own name, but with the property and as agent of Tenbrook, to whom he remitted the profits. Tenbrook attempted to show that Sides had no authority to order the particular kind of goods which Hubbard had sold him. This he was not allowed to do and Hubbard was allowed to recover the value of the goods. Hubbard vs. Tenbrook, 124 Pa. St. 291.

**316. Agent Must Not Have Adverse Interests.** One may not be an agent if in his duties or relations to others he would be compelled to assume inconsistent obligations. He owes loyalty to the interests of his principal, and he cannot discharge the duties of his position fairly when his own interests, or those of others whom he also represents, are adverse. He cannot act as agent for both parties in one transaction unless both know of his double agency. Should he attempt to do so he will forfeit his compensation.

EXAMPLE

Bell, a real estate broker, acted as the agent of McConnell to sell certain real estate. For this he was to receive two per cent of the price. He also acted as agent for Johnson, who desired to buy real estate of a certain description and was to receive all the reduction he could get below $5000. He thereupon arranged a sale of McConnell's property to Johnson for $4500. Proof of these facts defeated his right to collect his commissions from McConnell, or his $500 from Johnson, his interests having been conflicting. Bell vs. McConnell, 37 Ohio St. 396.

**317. Ratification** is the adoption by one person of the act of another, who without authority has acted as the agent of the first. It forms a means by which one may assume the liabilities of a principal *after* the performance of an act. Ordinarily the contract between principal and agent must precede the doing of the service for which the agency exists, but if after an unauthor-

ized act has been performed by one as an agent, the person for whose benefit it was done, accepts the act as his own, he becomes a principal.

EXAMPLE

Scott sold a quantity of iron rails, which were laid down by employees of a railroad company, under the direction of the engineering department. When he sued for the price, defense was made that the rails were purchased by the president of the railroad, who was without authority to bind the company, except by action of the directors. Scott was allowed to recover the price, however, the using of the rails with knowledge of the directors having been a sufficient ratification. Scott vs. Middletown etc. R. R. Co., 86 N. Y. 200.

**318. Notice to Agent as Notice to Principal.** All facts and information which come to the agent, with reference to the subject matter of the agency, are impliedly notice to the principal, since the agent stands in his place, and should inform his principal of all facts and conditions material to his employment. Knowledge received before the relation of principal and agent begins, or that acquired independent of, and outside the employment, does not serve as notice to the principal sufficient to charge him with knowledge of the facts, unless the agency be a general one.

EXAMPLES

1. Mrs. Hyatt desired to escape liability on a lease with Clark, which had been executed for her by her agent, Lake, on the ground that Clark was carrying on a business which she objected to, and which she had not known when the lease was made. Nothing was said in the lease as to the kind of business Clark was to conduct, and Lake had known all the facts, but had failed to communicate them to Mrs. Hyatt. The court did not allow Mrs. Hyatt to escape liability, she being presumed to know the facts which her agent, Lake, knew. Hyatt vs. Clark, 118 N. Y. 563.

2. Ames, a fire insurance agent, knew that Bates, whose property was insured, was a constant violator of the rules of the company, but did not inform the company at the time Bates took out an insurance policy, and continued to collect premiums. After a fire loss the company sought to escape liability on the ground of these violations of its rules. This it could not do. Pringle vs. M. W. A., 76 Neb. 384.

## REVIEW QUESTIONS

1. Dutch authorized his employee, Black, who was an infant, to indorse a note and further negotiate it. This Black did by writing across the back, "Dutch, by Black, agent." He then sold it to Whitney, and the maker failing to pay it, Whitney sued Dutch on this indorsement. Could he recover? Why?

2. Ames hired Bates as a clerk and allowed him to order goods, to answer letters concerning them, and to pay and receive money. Later Bates ordered goods from one of the firms with which Ames had been dealing, requested that they be delivered to a dock on the river-front, and then absconded with them. Ames refused to pay for these goods and was sued for the price. Was he liable? Why?

3. A put goods into the hands of B to sell, telling him to recommend them to his customers and to get the best price he could. B, without A's knowledge, made fraudulent and untrue representations as to the quality of the goods and thereby induced C to purchase and pay for them. B accounted for the money to A. C, on discovering the fraud, sued A for breach of warranty. Could he recover damages from A? Why?

4. It is the law in most states that the first person to record a deed from the owner of property in the office of the register of the deeds, or county recorder for the county in which the land lies, secures a good title, even against a previous purchaser who fails to record his deed, unless he knew of the prior deed. Ames owned a piece of land and deeded it to Bates, who did not record the deed. Ames, who was a rascal, later deeded the same land to Call, who knew nothing of the previous sale and recorded his deed. All the deeds were drawn by Johnson, an attorney, who acted in the first instance for Bates, and in the second for Call. May Bates claim the land against Call? Why?

## CHAPTER XXXIV

### AGENCY — Continued

**319. Relation of the Parties.** There are three persons concerned in the law of agency, *viz.*: Agent, principal, and third person. These each have rights, duties, and liabilities to the other two. Rights will not be discussed, for the duties and liabilities of one party are generally reciprocally the rights of the other. For convenience these duties and liabilities will be discussed in the following order:

I. Duties of Agent { 1. To his principal
2. To third persons

II. Duties of Principal { 1. To his agent
2. To the third persons

III. Duties of Third Person { 1. To agent
2. To principal

**320. Duties of Agent to the Principal.** The agent must be loyal to his trust. He must not have interests adverse to his principal's. He must account to the principal for the profits resulting from the contract of agency, less his own compensation. He cannot sell his own property to the principal without disclosing the facts, nor can he dispute the title of the principal to the subject matter of the agency. When acting as an agent, he is the impersonation of the principal and if this fact be remembered it will dispose of the problems which arise from the relation of principal and agent. When he acts adversely to his principal he becomes liable for the damage which he causes.

**EXAMPLES**

1. A confidential agent of a theatrical manager who had a lease on a theater, shortly before his principal's lease expired, secretly secured a lease of

the theater for a new term of years for himself personally. The theatrical manager could compel the agent to transfer the lease to him. Davis vs. Hamlin, 108 Ill. 39.

2. A principal employed an agent to buy certain mining stock for him at a price of not more than $150 a share, and at the lowest figure possible. The agent notified him that he had secured the stock at $150 a share and sent him stock of his own. On learning these facts the principal could return the stock and demand his money, and would not be compelled to pay the agent his commissions. Curry vs. King, 6 Cal. App. 568.

*Must obey instructions.* The agent is liable for any loss or damage which may be caused to his principal by a failure to follow reasonable and lawful instructions. The relation of agency depends upon a contract and in this contract the principal may make any conditions which he desires. He also has the right to direct the work which the agent is to perform for him. If no express conditions are specified, the agent must act according to established customs and usages. Any breach on his part will render him liable to the principal, who can sue and recover for the resulting damage.

EXAMPLE

Wilson, a collector, was directed to remit money by mail in denominations of $100, but he remitted a large package of bills of smaller denomination, which were lost. He became responsible for the loss to the principal, having failed to follow instructions. Wilson vs. Wilson, 26 Pa. St. 393.

*Agent must not be negligent.* The care, skill, and diligence required of an agent must be commensurate with the circumstances and nature of his undertaking. He must use the same degree of care as other persons employed in similar undertakings would employ. He is not an insurer against all loss, like a common carrier, but must use ordinary care at all times, and if injury results to his principal from a failure in this respect, he may be sued for the damage thereby occasioned.

EXAMPLE

Sears, an insurance agent, was ordered by his company to cancel fire insurance on a house which had become a dangerous hazard. Sears neglected to cancel the insurance and the house was destroyed, the company being compelled to pay the owner $1000 under the policy. The company was then entitled to recover this amount from Sears, it having been damaged by his negligence. Franklin Ins. Co. vs. Sears, 21 Fed. 290.

*To Act in Person.* Another duty of the agent to his principal is to act in person, except when authorized either by his principal or by an established custom to appoint sub-agents. When an agent appoints a sub-agent, the liability of the agent extends only to the use of care and prudence in the selection of the sub-agent, but does not extend to cover injuries or wrongs committed by the sub-agent which were due to no fault of his and which could not have been reasonably expected.

In case, for example, negotiable paper is left with an attorney or a bank for collection in another town or state, the attorney or bank, as agent, has the implied authority to forward the instrument to a sub-agent located at the place where collection must be made. The agent and forwarder discharges his duty when he selects a suitable and reputable sub-agent to collect, and will not ordinarily be held responsible* for neglect or misconduct on the part of the sub-agent.

EXAMPLES

1. Ames was employed to manage a piece of real estate, keep it in repair, and to sell it for a price which he deemed suitable. He set a price and employed Bates to find a purchaser at that price. This was not a violation of the duty which Ames owed to his principal, as Bates had not been empowered to use any discretion. Penwick vs. Bancroft, 56 Iowa 527.

2. A bank in Burlington, Iowa, received a draft for collection against a New York party. This it forwarded to the Metropolitan Bank of New York for collection, but the latter bank failed to present and protest it in proper time and the indorsers were thereby discharged. For this damage the owner sued the bank in Burlington, Iowa, but was denied recovery, his only remedy being against the New York bank, which alone had been negligent. Guelich vs. National State Bank, 56 Iowa 434.

*Duty to Account for Money and Property.* It is the duty of the agent to keep correct accounts of his transactions, and to account to his principal for all money and property which come into his hands belonging to the principal. He must not mix the principal's funds with his own, and if he does, he will be responsible for any resulting loss. He must, when required, account for the profits of all transactions in which he acted, or should have acted, as the agent of his principal.

* In New York, Michigan, Ohio, Indiana, and New Jersey, however, the first agent is held liable for any damages, whether these were caused by his own negligence or not.

EXAMPLE

An agent collected money for his principal and placed it in a money drawer together with some of his own money, not in separate packages. All the money was stolen without the agent's fault. He was compelled to repay the amount to the principal, because his act of mingling the principal's money with his own made him the debtor, and no longer the agent, of the principal. Naltnor vs. Dolan, 108 Ind. 500.

*Duty to Give Notice.* It is also the duty of the agent to give timely notice to the principal of all facts coming to his knowledge and relating to the subject matter of the agency which it is material for the principal to know for the protection of his interests.

EXAMPLE

Burbridge was the agent of Devall, operating a steamboat for the latter. While the boat was being thus operated it was seized on a levy under execution by creditors of Devall and sold at public sale for $1000. The boat was reasonably worth $8000, and had Devall known of the seizure and sale he could have bid on it and prevented the sale of his property at a gross sacrifice. Devall was allowed to recover damages for the amount of his loss from Burbridge, whose failure to give notice was responsible for the loss. Devall vs. Burbridge, 4 W. & S. (Pa.) 305.

**321. Duties of Agent to Third Persons.** The ordinary purpose of the agent is to bring his principal into relations and obligations with third persons, but not to bind or obligate himself personally. He may, however, so conduct himself as to incur a personal liability. The agent is personally liable for injury to third persons when he acts beyond the scope of his authority, or when he makes contracts in his own name and not that of the principal. He is also personally liable for any fraud, assault and battery, or other civil wrong, committed by him, even though he is acting for the principal at the time.

EXAMPLES

1. Pitcairn was a fire insurance agent and wrote a policy for Kroeger, the policy providing that the insurance should be void if any gasoline were kept on the premises without written permission. Kroeger called attention to the fact that he always kept a small amount on hand. Pitcairn informed him that no written permission was required where so small an amount was kept and Kroeger accepted the policy on this basis. A fire destroyed Kroeger's building and he could not recover for his loss from the insurance company, on account of the keeping of gasoline without permission. He was, however, allowed to recover his damages against Pitcairn personally for the misrepresentation. Kroeger vs. Pitcairn, 101 Pa. St. 311.

2. While Osborne was at work as a carpenter in a manufacturing plant, Morgan, the superintendent, negligently suspended a tackle block above him in such a way that it fell and injured him. Osborne was allowed to recover from Morgan for his injury, even though the latter was merely the agent of the corporation which employed them both. (130 Mass. 102). In many states where the so-called "Employers' Liability" acts are in force, one workman injured by another can sue the employer, instead of the fellow-workman, for damages.

*When Agent Exceeds Authority.* If an agent exceeds both his real and apparent authority in making contracts for his principal, the principal will not be bound thereby. The agent, however, will be personally liable for any damages which may have been suffered by the party with whom he made the contract by reason of his wrongful act.

**EXAMPLE**

Adams was authorized to sign a note for Burnham for $400 payable in six months, payable to Anderson if Anderson would advance this amount. Adams secured the money and signed a note payable in sixty days to Anderson. This act was in excess of authority and Burnham did not thereby become liable on the note, whereas Anderson could recover from Adams any damages which he suffered, in this case $400 with interest. Anderson vs. Adams, 43 Ore. 621.

*Acting for an Unknown Principal.* In order to escape personal liability, the agent must disclose to third persons with whom he deals that he is an agent merely, and not the principal. If he conceals the fact that he is but an agent acting for another, or fails to reveal the identity of his principal, those who deal with him can hold him personally liable on contracts, as any credit which may be given in such events plainly extends to the agent, known to them.

**EXAMPLE**

Amans sued Campbell for wages on a contract which he had made with Campbell, as follows: "I hereby agree to work for Campbell & Co. during the logging season of 1896 at $80 a month, etc." Campbell was merely the agent for the McCord Lumber Company, which fact was unknown to Amans at the time of the employment. Amans was allowed to recover against Campbell personally. Amans vs. Campbell, 70 Minn. 493.

An agent may also become personally liable by failing to use care to show that he is acting merely as agent for another in the manner in which he signs his name. The proper way for an

agent to sign a contract for his principal is in form similar to the following: "Amos Black, by George Wheeler, his agent." The same result may be accomplished by merely signing the name of the principal, but should the agent sign his own name alone, or sign his own name as agent, but not add that of his principal, he will fail to bind his principal and any liability will be personal with him.

## REVIEW QUESTIONS

1. Hayden was employed by Rose to buy lands for him in Grant county. Hayden went to Grant County, bought some very desirable lands for himself, and procured other land nearby, not so good, for Rose. What rights, if any, would Rose have in the lands purchased by Hayden? Why?

2. Ames directed Bates to buy a large quantity of grain for him for immediate delivery. Bates bought the grain, took a warehouse receipt for the amount purchased, and delivered this to a carrier with instructions to forward the grain at once. The elevator in which the grain was stored burned before it was removed and Ames sued Bates for the loss. Could he recover? Why?

3. Brazil was the agent of Corcoran. Without disclosing this fact he ordered goods of Bryan, who agreed to sell them on credit, to be delivered within thirty days. After making this agreement, and before delivery, Bryan discovered the agency of Brazil, but nevertheless delivered the goods. Later he sued Brazil for the price. Brazil proved the facts stated and claimed they constituted a defense. Could Bryan recover? Why?

4. Kerfoot owned certain land and employed Hyman to sell it. Hyman bought it himself, concealing that fact, and taking the title in the name of a third person, but for his own benefit, and at the same time resold half of it for more than he had paid for the whole. Has Kerfoot any rights against Hyman? What?

5. Martine, an attorney, was employed as an agent to lend moneys on first-class bonds and mortgages. He made a number of loans to parties who were insolvent and took mortgages on property already heavily mortgaged, reporting such loans together with the names of the borrowers and descriptions of the properties mortgaged, to his principal, Mrs. Whitney, a widow, who two years later sued him for damages. May she recover? Why?

## CHAPTER XXXV

### AGENCY — Continued

**322. Duties of Principal to Agent.** The chief duties of the principal to the agent are (1) to pay him his compensation, and (2) to protect him against loss or injury sustained in the performance of his duty.

**323. Agent's Right to Compensation.** The principal must pay the agent the proper compensation for the services rendered. The amount of this compensation may depend upon the contract between the parties, or if no mention is made of the amount of compensation, upon the reasonable value of the services rendered. The promise of a principal to pay an agent is always implied. This rule does not apply, however, when the services were rendered as a mere act of kindness, without expectation of payment, such as are ordinarily freely performed by members of a family for each other; and the agent will be entitled to compensation in such cases only by express contract.

EXAMPLES

1. Wilson performed services for Dame without special authorization. Dame, however, had desired the particular services and Wilson had performed them expecting to be paid. After Wilson had completed his work, Dame accepted the benefits and otherwise ratified Wilson's acts. He was thereupon compelled to compensate Wilson for the reasonable value of the services. Wilson vs. Dame, 58 N. H. 392.

2. Wallace was employed as an agent of Floyd for one year at an agreed salary. At the end of the year he continued to perform the same work for another year and then sued Floyd for the reasonable value of the services, which was a larger amount than the original agreement had stated. He was allowed only to recover the amount stated in the contract for the first year, as compensation for his continued service, it having been his duty to notify Floyd if he wished to alter or enlarge the contract. Wallace vs. Floyd, 29 Pa. St. 184.

*When Compensation is Earned.* If the parties contract in reference to the conditions under which, or the time at which,

the compensation of the agent shall be due, such contract controls. In the absence of special mention of these matters in the agreement, the agent's compensation will not be considered to be earned until he has fully completed the thing which he was to do. When the undertaking is completed, however, the agent becomes entitled to the payment for his services, even though the principal refuses to accept the benefit, or has failed to be benefited by the work. This question most frequently arises in connection with sales of real property, when a broker has been employed to find a purchaser. The broker becomes entitled to his commission when he produces a purchaser who is able and willing to buy, on the proposed terms, even though the principal does not complete the sale.

EXAMPLES

1. Gelatt was employed by Ridge to find a purchaser for his business block for $23,000, Gelatt to receive a commission of $1400 for the sale. The next day Gelatt produced Brady who was able and willing to buy the property at that price, but Ridge increased his price and the deal was not consummated. Gelatt was nevertheless entitled to his commission, having done all that he was employed to do. Gelatt vs. Ridge, 117 Mo. 553.

2. Peter employed Barthell to find a purchaser for certain property, which he described, at a specified price. Barthell produced a purchaser who was able and willing to pay the price, but the sale was not completed, Peter in the meantime discovering that his own title to the land was defective and that he could not transfer a valid title. Barthell was, however, entitled to his commission. Barthell vs. Peter, 88 Wis. 316.

*If Agent's Authority is Terminated.* If the contract of agency has not been made for a definite time, the principal may terminate the employment at any time, upon paying the agent for his services up to that time. When an agent has been employed for a definite period, however, and his authority to act for his principal is terminated without good cause before that time, he may either (1) recover the reasonable value of his services to that time, regardless of the contract; or (2) recover for the damages he has suffered in an action for breach of contract. When an agent abandons his undertaking without good cause, he may recover for the services previously performed, less the damage which his abandonment of the contract has caused his principal.

EXAMPLES

1. Miss Howard contracted to serve as an actress for Daly, a New York opera manager, for a winter season, at $10 a week. She appeared at the proper time, but Daly had withdrawn the play in which she was to have appeared. She sued and was awarded $140 as being the loss which she had suffered. Howard vs. Daly, 61 N. Y. 362.

2. Diefenback was employed for six months by Stark at a salary to be paid for the entire term. At the end of four months Diefenback quit work without cause and sued for two-thirds of the agreed compensation. He could recover nothing. Diefenback vs. Stark, 56 Wis. 462.

*Note.*— The Wisconsin rule noted in the above case is severe in preventing any recovery where the agent abandons his undertaking without cause. A more liberal rule prevails generally entitling the agent to recover for services less the amount of damage caused his principal.

*Right of Agent to Reimbursement and Indemnity.* The agent is entitled to be repaid any expenses he incurred in carrying out his principal's business, when such expenses were properly incurred within the scope of his employment. No expenses can be collected from the principal, however, when they become necessary because of the agent's negligence, nor can he claim expenses when his services were to be performed for a gross sum.

If in the performance of an authorized act for the principal, the agent invades the rights of others, the eventual loss should fall upon the principal, not the agent. In such cases, should the agent be compelled to pay damages to the party injured, he will in turn have a right to claim indemnity from his principal.

EXAMPLES

1. Ames is employed as an agent by Bates to sell a quantity of goods on a commission of ten per cent. Bates ships the goods to Ames, who is compelled to pay storage charges before finding a purchaser. He is entitled to be repaid for these charges from Bates.

2. Moore was ordered by Appleton, his principal, to cut timber on certain land, which he supposed to belong to Appleton. The land belonged to Johnson, who sued and recovered damages against Moore. Moore in turn could recover against Appleton, his principal. Moore vs. Appleton, 26 Ala. 633.

*Lien.* For their compensation, agents have a right of lien upon the property which is the subject matter of the agency. The nature and extent of such lien is governed by statutes in the several states, which vary considerably.

*Right to Protection from Injury.* The agent is entitled to be provided with a safe place to work and safe instruments with which to work. The right to protection has come to the attention of the courts more frequently in controversies between an employer and his servant, than between a principal and his agent, but the rules which must be observed are similar. The employer owes to his servant the duties of providing him with (1) a safe place to work; (2) safe tools and machinery; (3) proper instructions from competent superiors, and (4) competent fellow workmen. If the servant is injured because of the failure of the master to provide any of these things he may recover for the injury from the master, unless he has contributed to the injury by his own negligence. The servant may be compelled to bear the liability, however, if he knows the machinery to be unsafe and fails to report the fact, in which event he is said to have assumed the risk.

Statutes have recently been passed in many states, and also by Congress, known as "Employers' Liability Acts," which further define the duties of the master to his servant and the principal to his agent. These statutes vary and are too technical to be discussed in detail in this work. Their general tendency is to extend the liability of the master and principal, and to protect the servant or agent, by denying the master and principal defenses which he was allowed by common law, among these being that the injury was caused by (1) contributory negligence; or (2) a fellow servant; and (3) that the servant or agent had assumed the risk.

**324. Duties of Principal to Third Persons.** Since the very function of agency is to create rights in third persons against the principal, or in the principal against third persons, through the medium of an agent, it may be stated as a general rule that the principal becomes obligated to third persons by any acts, or contracts, done or made in his behalf by an agent acting within the scope of his authority express or implied, or which have been subsequently ratified by the principal.

It has been noted that an agent may contract with third persons in the name of his principal, in which event the contract is said to be made with a *disclosed* principal; or he may not have

revealed the identity of the person for whom he was acting as agent, in which event the principal is an *undisclosed* principal. It is convenient to discuss the rights of third persons against these two classes of principals.

*Rights against Disclosed Principals.* A disclosed principal is liable to third persons for all the lawful contracts of his agent, made for the principal and in his behalf, while the agent was acting within the scope of his authority and in the course of his undertaking; or which have subsequently been ratified by the principal with full knowledge of the facts. By the term "scope of the authority" is meant the extent of the powers expressly or impliedly conferred upon the agent.

**EXAMPLES**

1. Johnson, a salesman traveling for Mathias, hired a livery team from Huntley, overdrove them, injured them, and Huntley sued Mathias for the damage. He was allowed to recover, the hiring of the team having been for the business of Mathias and within the authority of Johnson. Huntley vs. Mathias, 90 N. C. 101.

2. Marston sued Pickert for breach of warranty on a shipment of fish, which he had purchased from a salesman employed by Pickert, relying upon the salesman's representation that the fish would reach LaCrosse in good condition. Pickert claimed that he was not liable, as the salesman had no authority to make such warranties. Marston was allowed to recover, it being customary for such agents to "be authorized to do whatever is usual to carry out the purpose of their agency." Pickert vs. Marston, 68 Wis. 465.

*Against Undisclosed Principals.* It is the general rule that the real principal in a transaction, though undisclosed at the time of making the contract, may be held liable, when discovered, upon all simple contracts made in his behalf by his agent, even though at the time of making the contract the party dealing with the agent did not know that he was an agent or did not know who his principal was, and gave credit to the agent supposing him to be the principal.

**EXAMPLE**

Kayton sold goods to Bishop for $4500. Bishop was really acting for Barnett, but did not disclose that fact, Kayton having declared that he "would not sell a dollar's worth of anything to that man Barnett." Barnett received the goods. Kayton later discovered this fact and sued him for the price. This he was allowed to recover. Kayton vs. Barnett, 116 N. Y. 625.

*Responsibility for Agent's Acts.* Any principal is responsible for the lawful acts performed for him by his agent, with his authority. Third persons have a right to rely on an agent's apparent authority and are not bound by secret instructions and restrictions.

EXAMPLE

McNear appointed Johnson his general agent to sell horses, instructing him, however, not to warrant the soundness of one particular horse. In violation of instructions Johnson warranted the soundness of that horse, selling it to Browning, who discovered that the horse was unsound and sued McNear for breach of warranty. He was allowed to recover his damages. Browning vs. McNear, 145 Cal. 272; Aldrich vs. Wilmarth, 3 S. Dak. 525.

This responsibility extends also to wrongful acts committed by the agent while the agent is acting in the execution of his undertaking and within the scope of his authority. It is not to be assumed, however, that the principal is responsible for every act which his agent may commit. If the agent has finished that which he was authorized to do, or if he leaves the principal's affairs to attend to some matter of his own, and then commits an act which injures a third person, the principal will not be responsible.

The principal will not ordinarily be held *criminally* liable for the acts of his agent, unless he has in some way participated in, countenanced, or approved the act; but he may become liable to a penalty for permitting his agent to perform acts which a statute has imposed a penalty for performing. If, for example, a statute forbids, under penalty, the sale of liquors to minors, or the keeping of saloons open on Sunday, the principal will be liable for the penalty if the forbidden act be done by the agent, even though the principal had no knowledge of it.

EXAMPLES

1. Richberger went to an express office to procure a refund of money due him by reason of overcharges made by an agent of the company. While paying over the money and securing a receipt, the agent cursed, abused, and maltreated Richberger. The company was liable to pay Richberger damages for these acts. Richberger vs. American Express Company, 73 Miss. 161.

2. Amanda Craker was a passenger on a railroad. While traveling the conductor of the train molested her and kissed her. She sued and recovered damages from the railroad company for this assault, although the conductor was obviously acting outside of the scope of his authority. Craker vs. C. & N. W. R. R. Co., 36 Wis. 657.

## REVIEW QUESTIONS

1. Bonsall paid Wagner $1000 for Wagner's promise to deliver 5000 barrels of petroleum oil to him within thirty days. He relied on Wagner's credit alone. The oil was not delivered in the time promised, and Bonsall then discovered for the first time that Wagner was the agent for Beymer, and had made the contract for Beymer's benefit. Could Bonsall recover from Beymer for breach of contract for failure to deliver the oil? Why?

2. Komorowski sued Krumdick for the price of wheat which he claimed he had sold to Krumdick through Krumdick's agent, Grist. Krumdick proved that Grist had been his agent only to purchase wheat for cash, that this wheat had been sold to Grist on credit, that they had never received the wheat, and that there was no custom allowing such agents to purchase goods on credit. Could Komorowski recover? Why?

3. Wilson contracted to teach school for ten months at a given sum per month, but at the end of six months the school authorities, without reason, closed the school. Wilson sued for damages. What, if anything, could he recover? Why?

4. Dalton, while stealing a ride on the freight train of the Acme Railroad, was kicked off the train by Murphy, a conductor, falling in such a manner as to break both his legs. He sued the company for damages, the company proving that it had a rule that any conductor acting in this manner should be immediately discharged and that Murphy had been discharged. Could Dalton recover damages? Why?

5. Sarah Hill cared for her father during a long period of sickness, and on his recovery sued him for her services as a nurse. She had always resided in her father's household up to the time of commencing the suit. Could she recover? Why?

## CHAPTER XXXVI

### AGENCY — Continued

**325. Liabilities of Third Persons to Agent.** *On Contracts.* The agent usually has no right of action on contracts made by him for his principal. He is merely acting for the principal and both the rights and duties which he creates are ordinarily on behalf of his principal. If, however, the agent does not disclose the fact that he is acting for a principal, he acquires a right to sue personally to enforce the contract.

EXAMPLE

John Deitz sued an insurance company for a fire loss, he having taken out the insurance policy in his own name on some property belonging to his sister. It was admitted that if Deitz recovered he would have to pay the money over to his sister, and the only question was whether the suit should have been brought in the name of the sister, who was the principal of Deitz. The court decided that Deitz might sue as he had not disclosed the fact that he was merely an agent when he made the contract of insurance. Deitz vs. Insurance Company, 31 W. Va. 851.

*For Wrongful Acts.* The agent may recover damages for injuries to the property of his principal, and in such cases he must account to the principal for the proceeds. In some states, however, this right is limited to cases in which the agent has a personal interest in the property.

EXAMPLES

1. Whittemore circulated slanderous stories about Weiss, a salesman, so that Weiss was unable to negotiate sales with many of his former customers. This was not only an injury to the employer of Weiss, but also a personal injury to him, and he could recover damages against Whittemore. Weiss vs. Whittemore, 28 Mich. 366.

2. Holden, acting as agent, prepaid freight charges on goods belonging to his principal. The railroad failed to deliver the goods in good condition, and was liable to Holden for damages, he having a special property interest in the goods because of the advances he had made on them. Holden vs. Railway Company, 73 Vt. 317.

**326. Liabilities of Third Persons to Principal.** *On Contracts.* Little further need be said regarding the liabilities of third persons to the principal. It is fundamental that the principal may enforce all lawful contracts made with third persons by his agent, regardless of whether or not the fact that he was the principal was disclosed at the time of making the contract.

The principal also has the right to follow property belonging to him which his agent has wrongfully disposed of, acting outside of the scope of his authority, and to recover it from third persons. If an agent wrongfully disposes of goods which he had no right to sell, he is not really the agent of the principal in the particular matter, and the principal may recover them from a third person in whose hands they are, regardless of the innocence and good faith of the purchaser. If the agent disposes of money or negotiable instruments, however, the principal cannot recover them if they are in the hands of innocent holders for value. Purchasers have a right, however, to rely upon an implied authority of a general agent in all matters customarily handled by such agents.

EXAMPLE

Austin, a sales agent for Carr, a publisher, sold to Burton six typewriters used in Carr's office. The sale was without the knowledge of Carr. Carr was entitled to recover the typewriters.

*For Wrongful Acts.* The principal may recover damages for wrongs done or injuries committed to his property by third persons while the property is in the possession of an agent, in the same manner as though no agency had existed. A third person may also become liable to a principal if he maliciously interferes with the agent in the performance of his duties, or wrongfully induces the agent to abandon the work which he is bound to perform for his principal. He may further become liable in damages for false representations made to the agent for the purpose of inducing him to contract for his principal, or for entering into a conspiracy with the agent to defraud the principal.

EXAMPLES

1. Hunt maliciously caused the arrest of Collins, a railroad engineer, while Collins was running his train. This caused a congestion of traffic and the railroad was entitled to recover damages against Hunt. Railroad Company vs. Hunt, 55 Vt. 570.

2. Simmons, a member of the water board of the city of Boston, with authority to purchase land for a reservoir, entered into an agreement with Wilson, by which Simmons agreed to use his influence to secure the purchase at an increased price of land which Wilson bought, and to share half the profits. The city of Boston on learning of these facts sued Wilson and recovered damages. City of Boston vs. Simmons and Wilson, 150 Mass. 461.

**327. Dissolution of an Agency.** The relation of principal and agent may be dissolved or terminated in any of the following ways:

I. By Original Contract
1. By lapse of time
2. By accomplishment of object

II. By Act of the Parties
1. Principal
2. Agent

III. By Operation of Law
1. Death
2. Insanity
3. Bankruptcy
4. Marriage
5. War

**By Original Contract.** If the agency was originally created to endure for a given period, or until a certain act should be performed, the expiration of that time, or the performance of the act, terminates the agency.

EXAMPLE

Moore employed Stone to purchase a certain piece of real estate for him. This Stone did, Moore paying the price and paying Stone his commissions. Some months later Stone purchased the same property at a sheriff's sale and in an action by Moore to recover the land he claimed that Stone was his agent and that the purchase was made in his behalf. Stone was entitled to the property, however, the agency having terminated before his second purchase. Moore vs. Stone, 40 Iowa 259; Short vs. Millard, 68 Ill. 292.

**By Act of the Parties.** The principal may revoke the agency at any time, provided the agent's authority is not coupled with an interest in the subject matter, as when the agent has paid for the right to exercise the powers of the principal, or has been given property to sell with the understanding that the proceeds of the sale are to be used to satisfy a debt due to him. Although the principal has this *power* to revoke the agency at any time,

except where it is coupled with an interest, he does not always have the *right* to so so, and if he terminates the agency in violation of the original contract of agency, he becomes liable to the agent in damages. The principal may revoke an agency, for the improper conduct of the agent, without liability for damages.

EXAMPLES

1. Ames gives Bates authority to sell property for him, and from the proceeds to retain enough to satisfy a debt due him from Ames. This is an agency coupled with an interest, which Ames can not revoke. Marizon vs. Pioche, 8 Cal. 522.

2. Ames agrees to hire Bates for a period of six months, to sell goods. Ames wrongfully terminates the contract at the end of two months. This he has the power to do, and Bates cannot continue to work for him, but Bates may recover all the damages which he has suffered because of Ames' wrongful act. Stinsgaard vs. Smith, 43 Minn. 11.

Just as the principal has the power to revoke the agent's authority, so an agent may, at will, terminate the agency, subject to his liability for damages if the termination is without just cause and involves a breach of the contract of employment. The agent may, however, be justified in terminating the agency; this would be true if he were required to do an unlawful act.

EXAMPLE

Ames agrees to act as sales manager for Bates for a period of one year, but at the end of six months quits his employment to accept a better position with a rival concern. Ames is liable in damages to Bates for the injury caused Bates. Barrows vs. Cushway, 37 Mich. 481.

**By Operation of Law.** The changes in the condition of the parties which may work a termination of the agency are five in number. The *death* of the principal or of the agent terminates the agency, except in case the agency is coupled with an interest, in which case it survives the death of either party. Similarly, the *insanity* of either party will terminate the contract of agency as to all persons having knowledge of the insanity. If the principal becomes a *bankrupt* the agency is dissolved, and if a business agent becomes bankrupt the principal is freed from further liability, though if the agency was for the performance of formal acts not involving any discretion in the agent, his bankruptcy does not dissolve the relation. At common law, *marriage*

revoked all previous agencies created by the woman; at present, with her power to manage her separate estate, this result does not generally follow. The outbreak of a *war* between the respective countries of the principal and agent will terminate an agency, for business transactions between the two become practically impossible.

EXAMPLES

1. Wilson's agent had authority to draw money from a bank, deposited in the name of his principal. The bank honored a check drawn by the agent after Wilson's death. This was unauthorized and the bank was responsible to Wilson's estate for the amount of the check. Farmer's Loan & Trust Co. vs. Wilson, 139 N. Y. 284.

2. After Ames became insane, his agent, Bates, made a contract with Call, who knew of Ames' condition, and another one with Dale, who was ignorant of it. Call could not enforce his contract, while Dale could do so. Davis vs. Lane, 10 N. H. 156; Hill vs. Day, 34 N. J. L. 150.

3. Ames became bankrupt, and without knowledge of that fact, Bates, his agent, made a contract in Ames' name. The contract could not be enforced. Wilson vs. Harris, 21 Mont. 374.

4. Ames was an agent in Spain for an importing house in New York at the outbreak of the Spanish-American war. The agency was terminated, as business relations between the two countries became impossible. Williams vs. Paine, 169 U. S. 55.

**328. When Dissolution Takes Effect.** An agency is terminated as far as the agent is concerned as soon as he is notified of the termination, except in the case of death, when it terminates as to all parties at the instant of death. As to third parties, the rule is the same; the agency terminates as soon as they have notice of it. For this reason, the principal should, upon terminating an agency, give notice to all third persons who have had dealings with the agency; otherwise, he may become liable on future contracts made with them by his agent before their knowledge of its termination.

EXAMPLE

Lampson represented that his agent had extensive powers in the management of his business for an unlimited time, and later revoked the agent's authority, but failed to give notice subsequently to third parties who had dealt with him through the agent. The agent subsequently made a contract for Lampson with Tier. Lampson was bound on the contract with Tier. Tier vs. Lampson, 35 Vt. 179.

## REVIEW QUESTIONS

1. Wilson was the agent for Baker, keeping both his personal and the agency account in the New York National Bank. The agency account was kept under the name of H. Wilson, Agent, the bank being informed that he was acting for Baker. The bank pressed Wilson for payment of a note which he personally owed to it, and he authorized them to apply money from the agency account on the debt. This was not authorized by Bates, who sued the bank to recover the money. Could he recover? Why?

2. Hunter, as manager of a municipal gas works, purchased coal from Lever, who had agreed to pay Hunter a commission of twenty cents a ton on coal purchased, in order to induce Hunter to purchase from him. Hunter purchased 1000 tons of coal from Lever for the municipality, after this, and upon Lever's refusal to pay the commission, sued him. Could he recover?

3. Mrs. Hennessey was engaged in the laundry business in Chicago, and on her refusal to enter into a combination to increase her prices, other laundrymen, among them, Doremus, induced several of her employees to quit work unexpectedly and without notice. She sued for damages, and Doremus contended that her remedy, if any, was against the persons who quit work, and not against him. Could she recover? Why?

4. Goldsmith, a shirt manufacturer, employed Turner as a salesman. It was orally agreed that the employment should be for a term of five years at a stated salary. Goldsmith's plant burned to the ground at the end of two years and was not rebuilt, and he did not further employ Turner, who sued him for breach of contract. Could Turner recover damages? Why?

5. Alworth sued Mrs. Seymour to compel the conveyance to him by her of one-half a tract of land. Mrs. Seymour had agreed with Alworth, who conducted an abstract office, that he should look up her title to certain land, and prosecute a suit for her benefit, paying all expenses to recover the land, and on the recovery of the land, he should be entitled to a one-half interest in it. Alworth began work and after he had spent $200 Mrs. Seymour terminated the employment without cause. It was admitted that the land was worth $25,000. What, if anything, could Alworth recover? Why?

## CHAPTER XXXVII

## PARTNERSHIP

- I. Sufficiency of Creation
  - 1. As between partners
  - 2. As affecting third persons
- II. Kinds
  - 1. Active
  - 2. Ostensible
  - 3. Dormant
  - 4. Limited
- III. Incidents
  - 1. Authority of partner
  - 2. Relations between partners
  - 3. Liability to creditors
- IV. Dissolution
  - 1. How effected
    - a. By agreement
    - b. By act of parties
    - c. By decree of court
    - d. By operation of law
  - 2. Result
    - a. Powers after dissolution
    - b. Distribution of assets
  - 3. Notice of dissolution

**329. Definition.** A partnership is the relation existing between two or more persons who have combined their property, labor or skill in the transaction of business for their common profit. The parties to this relation are called partners.

Partnership resembles agency in that each partner who transacts business for the firm is considered as an agent for it. Hence many of the principles of agency are likewise applicable to partnership.

**330.** The existence of the contract of partnership may be determined by the conduct of the parties as well as by their express language.

**331. Purposes.** The two purposes of the contract of partnership are (1) to bind the partners to bear the possible losses of the partnership business, and (2) to entitle the partners to share in the profits of the enterprise. A community of interest is created by the contract of partnership and the partners become jointly liable for the debts and obligations of the enterprise. This is the great hazard which individuals must assume when they enter a partnership, for not only can the money which they advance to the firm business be devoted to the payment of its debts, but if that is insufficient they may be forced to contribute to the paying off of creditors to the extent of their private fortunes.

**332. Conditions Essential to Formation of Partnership.** Before there can be a valid contract of partnership there must be (1) competent parties, (2) a legal object, or subject matter, and (3) a mutual assent of the parties.

*Competent Parties.* Any person may be a partner who is capable of making valid contracts. Aliens may be partners except in times of war. Infants and insane persons may be partners, but their contracts are voidable, and they may interpose the defense of infancy or insanity to relieve them of personal liability further than the money they have actually contributed to the assets of the firm. Married women, may, under the modern statutes, become partners with persons other than their husbands.

EXAMPLES

1. Beall, a minor, paid Adams $2900 to be admitted to Adams' business as a partner. The firm was not a success. Beall disaffirmed the contract of partnership, and sued to recover his money. This he was not permitted to recover, as he had enjoyed the benefits of the partnership, but he was permitted to escape all future liabilities. Adams vs. Beall, 67 Md. 53.

2. Vail sued Warren Winterstein, Alice Tallmadge, and others as partners and Mrs. Tallmadge sought to escape liability on the ground that she was a married woman. This she was not permitted to do as by statute she was capable of entering into contracts. Vail vs. Winterstein, 94 Mich. 230.

*Legal Subject Matter.* A partnership may be created to carry on any business which the partners might lawfully engage in if acting separately. Not only may there be a partnership for carrying on a mercantile business, but the partnership may be

for farming, mining, the practice of law, medicine, dentistry, or some other enterprise or profession.

Partnerships cannot, however, be created to engage in unlawful businesses or those opposed to public policy. Offices of public trust, in which individual responsibility is to be desired, cannot be executed by a partnership, nor can a partnership be formed to engage in gambling, to stifle competition and control the market, to aid a belligerent in time of war, or to defraud the customs or revenue departments of the government. If partnerships be formed for such illegal objects, the members cannot sue to enforce any contract tainted with such illegality, though actions may be brought against the members of such a partnership by a person who did not participate in the illegality.

EXAMPLES

1. Chester sued Dickerson, Reed, Jones, and Dewitt for fraudulent representations concerning the sale of lands, claiming that Reed had misrepresented the land and that all the parties were liable as partners. Dickerson, Jones, and Dewitt attempted to escape liability on the ground that no partnership could exist for such a purpose. The court permitted Chester to recover, for there may be a partnership in such undertakings as well as in dealings with personal property. Chester vs. Dickerson, 54 N. Y. 1.

2. McConoughy sued Craft as a partner for a division of partnership profits. It appeared that each of these parties had owned grain elevators in Illinois and had combined to raise the price of grain by secret agreements. It was for the profits derived from such agreements that this suit was brought. Recovery was refused as the contract of partnership was contrary to public policy. Craft vs. McConoughy, 79 Ill. 346.

**333. What Acts Create a Partnership.** Acts sufficient to create a partnership differ when the question arises (1) between the partners, and (2) between the firm and third persons.

**As Between Partners.** The actual intention of the parties governs. Mere community of interest, even as the owners of specific property, does not of necessity constitute the co-owners partners. Even the sharing of profits in a business, though it raises a presumption of the existence of a partnership, may be shown to have existed by some other contract than that of partnership.

EXAMPLE

Smith sued Bodine for his services as a salesman, which by agreement between the parties was to be ten per cent of the profits of sales made by him. The defense was made that the relation between them was a partnership and that Smith's only remedy was to bring an action in a court of equity known as *a suit for an accounting* to distribute the partnership property. Smith was allowed to recover, as the parties had intended no partnership. Smith vs. Bodine, 74 N. Y. 30.

The sharing in both profits and losses of a business is strong proof that the parties intended a partnership.

EXAMPLE

Smith agreed to investigate and locate desirable timber lands, reporting the same to Putnam, who if he approved should advance the money necessary to purchase the lands, he to be repaid with interest, and on the sale of the lands both Smith and Putnam to share equally in the profits or losses. This made them partners. Smith vs. Putnam, 107 Wis. 155.

**As Affecting Third Persons.** When persons have held themselves out as partners, in a particular business, and have thereby induced others to deal with them in that capacity, they cannot later assert that there was no partnership between them, and that one of them only is liable for the debts of the enterprise.

EXAMPLE

Clark sued Webster for a debt owed to him by the firm of Rigney & Webster. Webster denied that he was a partner of Rigney and proved that at the time the debt to Clark was contracted he had an agreement with Rigney that he should be responsible for only one-third of the firms debts. Clark, however, could recover in full from Webster.

**334. Kinds of Partners.** Partners may be either (1) active; (2) ostensible; (3) dormant; or (4) limited.

An *active* partner is one who is a partner for all purposes, both as to other members of the firm and as to third persons, being entitled to share in the profits of the business and liable for its losses.

An *ostensible* partner is one who is a partner in name only, allowing himself to be held out to third persons as a member of the partnership, when in fact he is not. As such he is not entitled to share in the profits of the enterprise, but may become

liable for the losses of the business to all third persons who have relied upon the use of his name.

A *dormant* or concealed partner is sometimes called a silent partner. He is not published to the world as a partner, but in fact is one. Being unknown as a partner, he is in a position to share in the profits of a prosperous business, and to avoid personal responsibility in case of a failure. His position is analagous to that of the undisclosed principal in agency, for should it be discovered that he is a partner he may be held liable for all debts and obligations of the firm in the same manner as though he had been an active partner.

A *limited* partner is one whose rights to share in the profits, and liability to participate in the losses, are limited. This limitation can be secured only when special statutes in the several states are complied with. (For instance, as to publication of notice, use of *Limited* as part of firm name, etc.) Ordinarily a partner is liable for the entire debts of the firm, although he may demand contribution from his fellows.

**335. Articles of Partnership.** It is not necessary that the contract of partnership be a formal written instrument, but in important undertakings it is better to have it so. If there be no written agreement, the law will imply the rights and duties of the parties from the nature of the business transacted, but if special provisions be desired, the agreement should be embodied in a written document, known as the "Articles of Partnership."

Among the incidents of a partnership is usually a firm name, though this is unnecessary. It is proper, however, for a partnership to adopt a firm name, under which to transact business, if it be desired. Restrictions are placed in New York and Pennsylvania upon the use of the name of a person not actually interested in the business, and upon the use of the term "& Co." in the firm name of a partnership, the latter being reserved for corporations. In other states, the latter term is quite frequently used as a part of the partnership name.

## Articles of Partnership

The following is a simple form of articles of partnership for George Baxter and Henry Olds, partners in the retail clothing business, in Galesburg, Illinois.

**This Agreement** *made this 17th day of August,* 1916, *by and between George Baxter and Henry Olds, both of Galesburg, Illinois.*

**Witnesseth** *that the said parties hereby agree to become partners in the business of selling men's clothing, furnishings, and other merchandise incidental thereto, at retail, under the firm name of "The Hub," for a term of five years from the date hereof, upon the terms and conditions hereinafter stated:*

1. *That the business shall be carried on at No.* 16 *John Street, in the city above named, on the premises where the same is now being carried on by George Baxter, or at such other place as the parties hereto may mutually agree.*

2. *That each of said partners shall contribute the sum of* $10,000 *to the said partnership, and that the said share of Henry Olds shall be paid in cash into the assets of said firm, and that the said share of George Baxter shall be paid by transferring to the said partnership all the goods, wares, merchandise and fixtures now located on said premises, together with the good-will of the business conducted by him heretofore.*

3. *That proper books of account shall be kept by the firm and that semi-annual dividends shall be declared, each of said parties sharing equally in any profits of the business.*

4. *That each party shall be at full liberty to draw* $100 *monthly for his own private use, on account, of his semi-annual dividend.*

5. *That neither party shall become bail or surety for any other person; nor lend, spend, give, or make away with any part of the partnership property; or draw or accept any bill, note, or other security in the name of said firm, except in the due course of the partnership business.*

6. *That at the expiration or termination of the said partnership, a valuation and similar account of the stock, effects, capital, and good-will, if any, of the said firm shall be taken, and the balance of such account then found to exist shall belong to the said parties in equal shares, and be realized and divided accordingly, and thereupon each party shall execute mutual releases to the other.*

7. *That in the management of the firm business, each of said parties shall devote his entire time, and shall not engage in any other business or undertaking without having first obtained the written consent of the other; that each party shall have an equal voice in the management of the business of said firm.*

**In Witness Whereof** *the parties have set their hands and seals the day and year first above written.*

In the presence of
*SCOTT CHAMBERS.*
*JASPER HORN.*

*GEORGE BAXTER.* [Seal]
*HENRY OLDS.* [Seal]

## REVIEW QUESTIONS

1. Valentine and Jordan, as partners, manufactured machinery. Desiring to borrow money, they secured $8000 from Meehan, a banker, agreeing to pay a note for that amount with interest at the end of a year, and also to give him as a bonus one-third of the profits for the year. At the end of a year the note was not paid and Meehan sued for the $8000 with interest. Defense was made that Meehan could not collect at law for this amount as he was a partner. Could he recover? Why?

2. Roberts represented to Cornhauser that he and Diamond were partners doing business under the firm name of M. E. Roberts & Co. Cornhauser sold him merchandise on credit, and it not being paid for sued both Roberts and Diamond. Diamond proved that he had not shared in the profits or losses of the business, but had merely allowed Cornhauser to use his name for a payment to him of $20. The account for which Cornhauser sued was $5000. Could Cornhauser recover? Against whom? For how much? Why?

3. Smith and Jones, together with Brown, a dormant partner, transacted business under the firm name of Smith & Jones. Gordon, who knew nothing of Brown's connection with the business, sold them $2000 of goods. Later, on discovering Brown's interest he sued the three — Smith, Jones, and Brown — for the value of the goods. Smith and Jones were both insolvent and if any recovery were allowed Brown would have had to pay the account. By the articles of partnership he was entitled to only a $\frac{1}{20}$ interest in the profits. What amount, if any, could Gordon recover? Against whom? Why?

4. A firm doing business under the name of "The Unique Clothes Shop" is composed of Johnson and Uttley. Explain how Warren may become a dormant partner and Morgan an ostensible partner.

## CHAPTER XXXVIII

### PARTNERSHIP — Continued

**336. Partner's Authority.** By entering into a partnership, each member confers upon the others the authority to act for him. Each partner has the right of an agent to bind the partnership in all transactions within the scope of the partnership business.

As each partnership has certain objects, or exists for the transaction of certain forms of business, third persons are expected to take notice of the general scope of the business. If, through one partner, they extend credit to the firm, or enter into contracts with the firm, which are obviously outside the scope of the partnership business, they will be assumed to have knowledge of this fact and can hold liable only the partner with whom they contracted, unless he had express or implied authority from his associates.

EXAMPLES

1. C. I. and C. C. Roosevelt formed a partnership for the purpose of refining sugar and advertised the fact in the newspapers. C. I. Roosevelt gave the firm note to pay for a quantity of brandy, and when the note became due both partners were sued. C. C. Roosevelt was not bound by this act of his partner, because it should have been apparent to anyone that incurring a debt for a liquor shipment was outside the scope of the partnership business. Livingston vs. Roosevelt, 4 Johns. (N. Y.) 251.

2. Sloan and Patten were partners, practising law. Patten gave a firm note to pay for office rent. Sloan could not be held on this note, on the ground that in a *non-trading* firm, such as this, neither partner has the implied authority to bind the firm on negotiable paper, and that any person dealing with them is charged with notice of this fact. Smith vs. Sloan, 37 Wis. 285. This distinction between the power of a partner in a trading, or mercantile firm, and a non-trading firm is generally followed when the right of a partner to bind the firm on negotiable paper is in question.

**337. When Partners May Bind Firm.** The firm is responsible for any acts, admissions, or representations of a partner transacting partnership business. Any fraud he may commit in such matters will bind the firm, for it has represented him to be

a person worthy of confidence, and further, it has derived the benefit of the fraud. A partner may give receipts for debts owing to the firm for value, and in the case of trading or mercantile partnerships may issue negotiable paper, binding the firm.

EXAMPLES

1. Rosenkrans and Weber were partners in the wholesale jewelry business in Chicago. Having sold a supply of goods to Barker, a resident of Iowa, which Barker failed to pay for, Weber, by fraudulent representations, induced him to go to Chicago and then had him arrested in an effort to make him pay for the goods. The arrest was wrongful and on his release Barker sued both partners for false imprisonment. Although Rosenkrans resided in Wisconsin, and knew nothing of the transaction, he was liable with his partner for the wrong done. Rosenkrans vs. Barker, 117 Ill. 331.

2. Luther and Frank Hess, partners in the practice of medicine, were sued by Isaac Lowrey for malpractice, he proving that one of the partners had treated his broken shoulder in a negligent and unskilful manner. Both partners were liable for the damage. Hess vs. Lowrey, 122 Ind. 225.

**338. When Partners May Not Bind Firm.** A man may not bind his partner or partners by giving a firm note or check in payment of his individual debt, for the nature of the debt is notice to all parties that in giving the firm's paper he is acting beyond the scope of his authority. He cannot dispose of the entire assets of the firm unless he has express authority to do so, or the other partners are inaccessible or incapable of acting and the matter is urgent. He cannot bind the firm by a guaranty of his own or another's debt, nor can he bind the firm to submit a disputed matter to arbitration.

EXAMPLE

Templeton and Sheets made a contract for the establishment of a stock farm and purchased a herd of mares for that purpose, together with a quantity of hay and feed. Without the knowledge or consent of Sheets, Templeton sold all the property to Lowman and a contest arose between him and Sheets as to the ownership in the property. Sheets retained his interest in the property, as the sale of the entire assets and plant was obviously outside the scope of the business, for it destroyed the business. Lowman vs. Sheets, 124 Ind. 417.

**339. Relations to Each Other.** As between themselves, the partners have certain rights and liabilities. If it be remembered that the partnership is a contract similar to the contract of agency these rights and liabilities will be readily understood.

A partner must act in good faith toward his co-partners and cannot make a secret profit in firm business. He must not engage in undertakings where his personal interests are antagonistic to those of the firm, and if he does so he may be called upon to account to the firm for the profits arising therefrom.

EXAMPLE

Ames, Bates, and Call are partners engaged in the real estate business. Knowing that the partnership is about to purchase a certain piece of land, Bates secures the title to the land and resells it to the partnership at a profit. If this was done without the consent of the other partners they are entitled to require Bates to account to the firm for the difference between the price he paid for the land and the amount which he received for it from the firm.

It is also the duty of a partner to transact the firm business with reasonable care, skill, and diligence; and he is responsible for loss resulting from any negligence on his part, unless it results from an honest and reasonable mistake in judgment.

EXAMPLE

Murphy & Crafts were partners, under an agreement not to indorse any note or draft, except for firm purposes. Crafts, in violation of this provision, and to accommodate a friend, indorsed a draft which passed into the hands of a holder in due course, and the friend failing to pay it at maturity, the firm was compelled to pay $5000. Murphy sued Crafts and was allowed recovery for the amount of his share of the draft. Murphy vs. Craft, 13 La. Ann. 519.

Each partner is entitled to share in the profits of the business in the proportion of his interest in the firm, and to be consulted and allowed to participate in decisions concerning important undertakings unless he has consented to leave the active management of the business in the hands of a managing partner.

EXAMPLE

Yorks and Tozer were partners in a single real estate transaction, a piece of property being purchased and the title taken in Tozer's name. Later Tozer, without consulting Yorks, a lawyer whose knowledge of the subject would have rendered the purchase unnecessary, purchased for a large amount of money an apparent but really unfounded claim against the real estate. This act was gross negligence and he could not require Yorks to contribute to this expense. Yorks vs. Tozer, 59 Minn. 78.

Each partner has the further right of contribution and indemnity from his co-partners. If, in consequence of his membership

in the firm, he should be required to pay debts of the partnership beyond the extent of his original contribution to the firm assets, he may require his partners to bear their *pro rata* share of the excess.

EXAMPLE

Johnson, Malone, and Hannan are partners engaged in the retail grocery business, each having contributed $3000. The Central Supply Company collects $4000 from the firm on a note for $12,000 which the firm owes it, and sues and recovers the $8000 balance from Malone, who may compel Johnson and Hannan each to reimburse him for one-third of this amount.

If a partnership be formed for a definite period and one of the partners without consent or cause withdraws before the end of the term the others may recover damages as for the wrongful breach of any contract.

**340. Rights of Creditors.** The creditor of a partnership has a right to be paid out of the assets of the firm, of if these be insufficient then out of the individual assets of the partners. An agreement between or among partners to release one of their number from this personal liability, however binding as among themselves, cannot be enforced against creditors.

The personal creditors of a member of a partnership may not only collect their debts from the personal assets of their debtor, but they may with certain limitations secure payment out of the debtor's share in the partnership assets. Their rights are secondary to those of the firm creditors, for otherwise a partner's share in the firm assets could be withdrawn to pay his private debts, leaving the responsibility for payment of the partnership debts upon the remaining partners. It is therefore generally held that the personal creditor of a partner can reach his debtor's share in partnership assets only by levying upon the partner's undivided interest in the firm assets, and demanding an accounting of the partnership in the course of which it is made clear that the interests of all the creditors of the firm are protected. The personal creditors may then be paid out of their debtor's share in the balance. The rights of personal creditors to partnership assets are governed largely by statutes which vary in the several states, and which should always be consulted.

The creditor of a partnership always has the option of enforcing payment of the debt either against the partnership or against

the individuals composing the partnership, but if he attempts to collect the debt out of the private assets of a partner his right is secondary to the right of personal creditors of that partner. Just as a partnership creditor has the right to demand that the firm assets be applied to the payment of his debt before they may be used to satisfy the personal debts of a partner, so have the personal creditors of a partner the right to insist upon being paid first out of the private assets of their debtor.

### EXAMPLES

1. A and B were partners in a trading firm. C obtained a judgment against A individually and an execution was issued. The sheriff could seize the entire property of the firm, and after an accounting between the partners had been had to determine their respective shares, could sell enough of A's property to satisfy the debt. Branch vs. Wiseman, 51 Ind. 1; Clark vs. Cushing, 52 Cal. 717.

2. A, B, and C were sued for a partnership debt, and judgment was obtained against them. The creditor could then levy either upon the partnership property or upon the private property of either of the partners, unless the latter's personal creditors intervened and insisted that the firm assets be first devoted to the payment of the debt. Much vs. Allen, 17 N. Y. 300; Fisher vs. Syfers, 109 Ind. 514.

3. A, a member of the firm of A & B, became a bankrupt. C, a creditor of the firm, sought to file his claim as a creditor of A and to secure a share of A's personal assets. This he was unable to do, as the private creditors of A were entitled to be paid first. Brock vs. Bateman, 25 Ohio St. 609; Halsey vs. Norton, 45 Miss. 703.

## REVIEW QUESTIONS

1. Hodge, Twitchell, and Rubey, who were partners, decided to purchase a lot on which to erect a building, for $2500, a fair price. Unknown to his partners Twitchell went to the owner who agreed that if Twitchell could secure him a purchaser for $2400 he would pay Twitchell $90. Twitchell reported to his partners the fact that the lot could be purchased for $2400, which purchase was made and the seller of the land paid Twitchell $90. On learning the entire transaction had Hodge and Rubey any further rights? What?

2. A did business under the firm name of A & B, with B's consent, but the property used and held out as firm property really belonged to A. A and B both became bankrupt. There were private creditors of both A and B, and creditors of the apparent firm of A & B. What were the rights of the three classes of creditors against the property held out as firm property?

3. A and B formed a partnership for three years to conduct an illegal gambling house. At the end of the time, all the money acquired in the busi-

ness was in the hands of A, who refused to pay over any of it to B. Could B recover his share from A?

4. Insley & Shire were partners. Insley attended to the details of the active business, while Shire looked into the affairs of the concern once a month, examining the books. Shire recommended the employment of Milligan as a bookkeeper. Milligan, by false entries in the books, embezzled $10,000, in the course of six months. During that period Insley had neglected his own supervision of the business and Shire, relying upon Milligan's honesty, had taken a trip to Europe. Milligan's fraud was so clever, however, that had both the partners devoted their attention to the business it was doubtful whether they would have discovered the fraud. Each partner sued the other for damages for carelessness and negligence. Which could recover? Why?

## CHAPTER XXXIX

## DISSOLUTION OF PARTNERSHIP

**341. When Liability Begins and Ends.** The liability of partners begins when the partnership is formed, which may be either when an express agreement of partnership is made, or when third persons extend credit upon the strength of the apparent relationship which parties allow to be inferred from their conduct.

If a person enters a partnership which is already in existence, he is not liable for debts incurred before his admission to the firm, unless he expressly or impliedly agrees to assume such liability. After a member retires from a firm he is not liable for future debts incurred after his withdrawal, except to former creditors who have not been notified of the change in the firm.

On account of this condition, by which the dissolution of a firm may relieve partners of further liability, other than for debts already incurred, it is of the greatest importance to determine the manner in which the dissolution of a firm may be effected.

**342. Dissolution, How Effected.** A partnership may be dissolved in any of the following ways:

I. By agreement
II. By act of one party
III. By degree of court
IV. By operation of law

**343. Dissolution by Agreement.** The contract of partnership is a voluntary one, and unless a definite time is set for its expiration, it may be terminated at any time by any partner. If, however, a time be set in the contract of partnership, it terminates accordingly, unless all the partners make a further agreement, express or implied, to continue it. If the partnership is formed to accomplish a particular object, it is terminated when the object is accomplished. Notice of dissolution should be given to all the creditors.

EXAMPLE

Hollander & Kirkwood became partners in the jewelry business for a period of one year from August first, and carried on the business until October of the year following. Kirkwood became dissatisfied, closed the store, and gave public and private notice that the firm had been dissolved. Later Hollander bought goods in the name of the firm and the creditors sought to hold Kirkwood liable. Kirkwood had the right to terminate the partnership and notice which was given to parties dealing with the partnership was sufficient. Solomon vs. Kirkwood, 55 Mich. 256.

**344. Dissolution by Act of One Party.** The other partners may demand a dissolution if one partner refuses to act with them, or if he engages in other business against their wishes. A dissolution is also effected if one partner sells or assigns his interest in the partnership. The other partners are not obliged to accept the purchaser or assignee as a new partner, because they may have strong objections to making him an agent of the partnership or entrusting its affairs in his hands, which would be the result if he was accepted as a partner. If such a purchaser or assignee is not accepted as a partner, he becomes a tenant in common with the others in the property of the partnership and is entitled to an accounting of the property, and a payment over to him of his interest.

Should a partner sell or assign his interest in, or otherwise terminate, a partnership created for a fixed period, before the agreed time of termination and without cause, he is guilty of breach of contract, and may be called upon to pay damages to the remaining partners for any injury caused them.

EXAMPLE

Harvey and Howell were partners in a retail store. Howell went to a wholesale house in Philadelphia and bought a line of goods at a very low price. On his return to his home, he discovered that prices in that line of merchandise were rapidly advancing, and gave notice to Harvey of the dissolution of the partnership, retaining possession of the goods and taking in his son as a partner. The prices continued to advance and he made a large amount of money. In an accounting between Harvey and Howell, Howell offered to pay Harvey the value of one-half the merchandise at the time of the notice of dissolution. Harvey, however, was entitled to damages for the termination of the partnership to the amount of one-half of the profits occasioned by the advance in price of goods, the dissolution not having been in good faith. Howell vs. Harvey, 5 Ark. 270.

**345. Dissolution by Degree of Court.** A court of equity will, for just and reasonable causes, decree a dissolution of a partnership, upon the petition of a member. When such a dissolution is decreed, a receiver is usually appointed, who takes charge of the firm's business, collects all debts due to it, pays its obligations, converts the assets of various kinds into money, and divides the balance according to the interest of each partner.

EXAMPLE

Gerard and Gateau were partners in the manufacture of zinc roofing. Gerard brought suit asking for a dissolution of the partnership on the grounds that Gateau was quick-tempered, was insolent and over-bearing to customers, had made overcharges for work which injured the reputation of the firm, and had employed as a salesman his nephew, whose work had caused the firm losses and finally necessitated his discharge. These grounds were held insufficient to prevent co-operation between reasonable men, and as the business was profitable and the period of ten years for which it had been formed had not elapsed, the court refused to decree a dissolution. Gerard vs. Gateau, 84 Ill. 121.

The grounds for granting a decree of dissolution are, in general, that it has become impracticable to continue the business. One of the partners may be unable to carry out his part fully, or the undertaking may be visionary; one of the partners may be so intemperate or immoral or unreliable as to imperil the success of the business, or he may have wrongfully excluded the others from their share in the management of the business, or may deny them access to books of account; and these wrongful acts will justify a court in ordering a dissolution of the firm and a distribution of its assets.

EXAMPLE

The firm of Groth and Payment was unable to succeed financially because one of the partners devoted a large part of his time to gambling and drinking, frequently staying away from the business for several days at a time, and frequently drawing large sums from the firm's account, to the detriment of the business. The other partner could secure a dissolution of the firm, even though the period for which it had been created had not elapsed, by a proceeding in a court of equity. Groth vs. Payment, 79 Mich. 290.

**346. Dissolution by Operation of Law.** Any change in the legal status of a partner, so that he is incapable of acting for

himself, will dissolve a partnership by operation of law, for the law contemplates, not only that partners shall be able to create contracts at the formation of the partnership, but that they shall continue so during its existence.

A partnership may be ended if a partner becomes insane or a spendthrift and is placed under guardianship. At common law the marriage of a female partner dissolved a partnership, but this is not true in states where married women may contract as though unmarried.

The death of a partner works a dissolution. This dissolution takes effect, like the dissolution of an agency in case of the death of the agent, immediately, regardless of whether or not third persons have notice of it. The representative or heirs of the estate can take no part in the management of the partnership business, without the consent of the surviving partners.

EXAMPLE

Bates, of the firm of Ames, Bates and Call, dies, and no notice of this fact, or of the dissolution of the firm, is given to creditors. Dale, who has dealt with the firm before, sells a shipment of goods to Ames for the firm, without knowledge of Bates' death. Being unpaid, he sues the estates of Bates and Call personally. He cannot recover against either as Ames alone is bound to pay, unless Call consented to a continuation of the firm as between himself and Ames. Schmidt vs. Archer, 113 Ind. 365.

**347. What Powers Cease by Dissolution.** When a dissolution occurs, there is a change in the relations of the partners and in their rights and powers. They can no longer use the partnership property for the purposes of trade, but can make only such contracts as look to a settlement of the partnership affairs. Neither partner can make or indorse negotiable paper in the firm name. Neither can create new obligations, or vary those already made except for purposes of collection.

EXAMPLE

After the dissolution of the firm of Fisk and Small, Fisk, one of the partners, signed a note in behalf of the firm for $500 payable to Jones, a firm creditor, who knew of the dissolution. The debt for which the note was given was about to outlaw and the giving of the note did not serve to bind Small nor extend Jones' rights against the firm assets after the time when the original debt would have outlawed. Gates vs. Fiske, 45 Mich. 522.

**348. What Powers Remain After Dissolution.** On the dissolution of a firm each partner has the right to collect and receipt in the firm name for all debts due the firm. Each also has the right to adjust and pay all unliquidated debts of the firm with the firm's money. Each may also sell the firm's property for cash, and each may insist that all firm debts be paid before any division of assets is made between the partners. The partners must continue to be diligent and to exercise good faith in closing up the affairs of the firm, and if either unreasonably prolongs the business, the court may be asked to intervene and appoint a receiver. Money may be borrowed, or property mortgaged or pledged, only in so far as it is necessary to preserve the assets of the firm for the purpose of closing up the business.

**349. New Powers Created by Dissolution.** When a partnership is dissolved, the peculiar relation of the partners, as such, ceases, and they become tenants in common in the property of the partnership, with undivided shares.

When the dissolution is caused by the death of one partner, his personal representative becomes a tenant in common with the surviving partner or partners. As such a tenant in common he has the right to have an accounting and division of the assets of the business, but has no right to a part in the winding up of the business as a partner. This is a right belonging solely to the surviving partners. They have the entire legal title to all the partnership assets, and they only can sue and be sued in respect to partnership matters. The survivor is virtually a trustee for the firm, but as such is not entitled to any special compensation for his services. The representatives of a deceased partner are entitled to their share in profits that result from winding up the business, and if the business is carried on with no effort to wind it up, they are entitled to profits, but are not liable for losses.

EXAMPLE

Hawkins was the surviving partner of the firm of Capron and Company. Capron's heirs took possession of some of the property of the firm, and refused to deliver possession of it to Hawkins, who sued them and was permitted to recover possession of all the firm property and to hold it for the purpose of winding up the business. Hawkins vs. Capron, 17 R. I. 679.

**350. Notice of Dissolution.** When a partnership is dissolved, notice of the fact should be sent to all with whom the firm has had credit in the past. This is for the protection of the retiring partner, not that he may avoid liabilities already incurred, but that he may avoid future obligations assumed by the remaining partners. Until notice is given to creditors of the firm, the retiring partner continues to be liable for future debts contracted with them, for the dissolution of a firm as to third persons takes place only when they have notice of it. When the dissolution occurs by operation of law, actual notice is not necessary, and third parties are presumed to have notice. The usual method of giving notice of dissolution is to send a circular letter to all who have previously extended credit to the firm, and to publish notice of the dissolution in a newspaper for the benefit of those who knew of the firm's existence and who have not dealt with it in the past, but who might do so in the future.

**351. Limited Partnerships.** The particular characteristic of all partnerships at common law was that each partner risked his entire fortune in the business, for he might be called upon to pay the entire debts of the firm. By statutes in the various states a new form of partnership called a limited partnership is now permitted in many states*. By conforming to the statutes it is possible for one or more of the partners to limit the extent of his liability to the amount of the firm capital which he actually contributed. Such partners with limited liability are called special partners, distinguishing them from the general partners. While the statutes of the various states differ, the following provisions are quite general:

1. There must be one or more general partners, and one or more special partners.

2. A certificate of partnership containing the name of the firm, its nature and object, the names of all the partners with their residences, a designation of who are general and who are

* Alabama, California, Connecticut, Florida, Georgia, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Montana, Missouri, Mississippi, New Jersey, New York, Pennsylvania, Rhode Island, South Carolina, South Dakota, North Dakota, Vermont, Virginia, Wisconsin.

special partners, together with the amount of the investment of the special partners, must be signed by all the partners, recorded in the county records and published for a specified time in a newspaper of general circulation in the community.

3. The names of the special partners must not appear in the firm name, and the word *Limited* or the abbreviation *Ltd.* must follow and be part of the firm name.

4. The investment of the special partners must be paid in in cash.

Unless the provisions of the statutes of the particular state in which it is attempted to form such a partnership are strictly observed, the firm will be treated by the law as a general partnership and the individual liability of all the partners will be that of general partners.

## REVIEW QUESTIONS

1. Youmans and Adams, partners, dissolved partnership. No notice of dissolution was given and thereafter Youmans in the firm name agreed to buy quantities of wheat of both Jones and Brown, both of whom were former creditors of the firm. Jones actually knew of the dissolution, but Brown did not. Upon Youmans' failure to carry out the contracts could Jones and Brown claim any liability on the part of Adams? Could either?

2. Ames and Bates were partners. Call bought an interest in the business, after which time Bates gave a firm note to Dale in payment of a debt contracted before Call became a partner. Call had no knowledge of this note until he was sued on it by Dale. Could Dale recover? Why?

3. Chastain and Harvey, a firm, dissolved partnership. Harvey, without any authority from Chastain, issued a note in the firm name to pay a debt which the firm had owed prior to its dissolution. Chastain was later sued on this note. Could recovery be had against him? Why?

4. A, B, and C are partners. A and B discover that C, who has been managing the business affairs of the firm, has kept the books fraudulently and misappropriated large sums of money to his own use. What remedies have they?

5. X, Y, and Z having dissolved the partnership which had existed between them, X undertook to settle up the firm business, and in the course of the settlement entered into an adjustment of account with A by which it was agreed that the firm was indebted to A to the amount of $1000; he also made a part payment on a debt of the firm to B which at the time of payment was barred by the statute of limitations. To what extent, if any, are Y and Z bound by these actions of X?

## PRACTICAL SUGGESTIONS

Remember that as a partner:

I. You are liable to the full extent of your own property for firm debts. If a judgment against the partnership cannot be satisfied out of firm assets, each partner will be individually liable for the full amount of the deficit.

II. Your partner has as much authority in the conduct of the firm business as yourself. Your credit is at the mercy of your partner.

III. Your partner's death, insanity, or bankruptcy immediately dissolves the partnership.

IV. You may desire to wind up your interest in the concern, but if your partner refuses to permit you to withdraw, you will have to resort to long and expensive litigation.

# CHAPTER XL

## CORPORATIONS

- I. Creation
  - 1. Procedure to incorporate
  - 2. Charter from state
    - a. By special act
    - b. By general act
- II. Management
  - 1. Stockholders
    - a. Common
    - b. Preferred
  - 2. Directors
  - 3. Officers and agents
- III. Dissolution
  - 1. Manner
    - a. Expiration of charter
    - b. Surrender of charter
    - c. Forfeiture of Charter
    - d. Repeal of charter
  - 2. Effect
    - a. As to stockholders
    - b. As to creditors

**352. Introduction.** The corporation is the most recent form of business organization. When the Federal Constitution was adopted, there were six corporations engaged in business in this country. Two of them were banking houses, two insurance companies, one a bridge company, and one was engaged in the manufacture of iron. There are now over five hundred thousand corporations in the United States, representing immense aggregations of capital and engaging in every conceivable form of business, of both a public and a private nature. The corporation is a favorite form of business organization for three reasons: First, because investors are not individually liable for all the debts of the corporation, as in the case of a partnership; second, because it offers a simple form of investment for the person who has some money but not enough to engage in a business for

himself, or who wishes to invest only a part of his fortune in a particular enterprise; third, because it offers a convenient means of engaging a large amount of money in a single enterprise, through the contributions of many investors.

**353. Definition.** A corporation is an organization the members of which, called stockholders, are authorized by law to act in certain respects as a single person, under a corporate name. Chief Justice Marshall defined it as "an artificial being, invisible, intangible, and existing only in contemplation of law," and this definition has persisted in judicial decisions. The corporation is composed of members, usually stockholders, but it is something entirely different from the members who compose it.

**354. Consists of Two Contracts.** The existence of a corporation is founded, not upon contract between the members composing it, as in a partnership, but upon a *charter*, or *franchise*, from the state, providing that the corporation may exist and act as an artificial person. This charter is really a contract between the state and the corporation. By this contract the state agrees that the corporation may exist, transact business, and exercise the powers for which it is organized.

There is also a contract between the stockholders. Since members' votes carry weight in proportion to the stock they own, the management and control of a corporation is in the hands of the members holding a majority of the stock. They elect officers and direct the business of the enterprise. But the majority of a corporation is always obligated by an implied contract that they will manage the corporation according to the provisions of the charter, and will not engage in prohibited or unauthorized undertakings, or employ the corporate funds for purposes other than that for which the corporation was organized. This restriction is for the benefit of the minority members of the corporation, and is in reality a contract between the members composing the corporation that the majority will always act within the charter powers.

EXAMPLE

The Acme Company, a corporation, is organized and receives a charter from the state empowering it to engage in the business of manufacturing iron rails. It is composed of a large number of members, and the majority of these

members vote to engage in the business of operating a railroad. The minority members may object to this and may prevent the majority members from engaging the capital of the corporation in such a business which is outside the scope of the powers of the corporation as represented by its charter. Or an objection might be raised by the State. Each member is entitled to demand that his contribution to the corporation shall be used for the purposes for which the corporation was organized and no other.

**355. Nature of a Corporation.** While the corporation is based upon these two contracts, it is not a contract itself, but a person. It is not a natural person like the members who compose it, but an artificial person with the power of acting in certain matters like a natural person. It possesses rights and duties very similar to those of a natural person. Among these are: (1) The right of property and reputation protected at common law, and under constitutional provisions, similar to the same right of natural persons; and (2) duties, arising both from the provisions of the charter by which it was created and as fixed by law. Among the secondary rights which a corporation possesses are: (1) The right to continue in existence after the death, withdrawal, or substitution of its members; (2) the right to take and hold property in its corporate name, such property belonging to the corporation, and not to the members who compose it; (3) the right to sue and be sued like a natural person; (4) the right to incur debts and make contracts in the corporate name, which create obligations binding upon the corporation alone and for the collection of which the corporate assets alone are liable; (5) the right to contract with its own members and to sue and be sued by them.

EXAMPLES

1. A candidate for public office in public speeches falsely accused a coal company, during the coal famine of 1902-3, of charging exorbitant prices for coal and refusing to sell at all to persons who were sick and suffering. Such charges amounted to slander, injured the company's business reputation, and entitled it to sue for damages which it had suffered. Gross Coal Co. vs. Rose, 126 Wis. 24.

2. A canal company was bound by its special charter from the state to construct a canal deep enough to accommodate certain vessels. It failed to keep the canal in a suitable condition, and a vessel was damaged through this negligence. The owner of the vessel was entitled to recover his damages against the corporation, it having been under a duty for the benefit of all persons who used the canal. Riddle vs. Proprietors, 7 Mass. 169.

**356. Kinds of Corporations.** The two important kinds of corporations in present day commerce are (1) Public, and (2) Private Corporations. Public corporations are primarily governmental institutions created by law for the administration of public affairs in particular communities. Such organizations are frequently called municipal corporations, and include cities, towns, villages, counties, school districts, drainage districts, and irrigation districts created by the state.

Private corporations are such as are created by private enterprise to accomplish some private end. They are usually organized for private profit, the members sharing in the profits to the extent of their shares in the corporation. They include religious, charitable, railroad, banking, insurance, manufacturing, and trading corporations. Even though they be formed for the purpose of serving the public generally, as is true in the case of railroads, water-works, and gas and electric companies, if they exist primarily for private gain they are private corporations. They can only exist by the consent of the members incorporating the company.

**357. Compared with Partnerships.** The features of this form of commercial organization are strikingly explained when it is compared with the partnership. The following are the chief differences between the corporation and the partnership. (1) *In creation:* Corporations can be created only by express authority of the state; partnerships, by mere contract of the parties. (2) *In franchise:* A corporation has at least one franchise, the franchise from the state to be a corporation; a partnership, none. (3) *In management:* A corporation is managed only through its duly appointed officers and agents; in partnerships, each partner, or member, can act for the partnership. (4) *In powers:* The corporation can lawfully exercise no powers except those expressly conferred by the state or necessarily implied from those granted to it by the state, and these cannot be enlarged without the consent of the state; while the members of a partnership may do any lawful thing which they agree to do. (5) *In duration:* The corporation is perpetual unless expressly limited—the death, resignation, or insolvency of members does not dissolve it; but any one of these dissolves a partnership. (6) *In*

*ownership of property:* The title to the corporate property is in the corporation and not in the individual stockholders; that of the partnership in the members of the partnership, they being considered joint owners. (7) *In litigation:* A corporation sues or is sued in its corporate name; the partnership, in the names of its members. (8) *In transfer of interest:* The transfer of his interest by a member has no effect on corporate existence; but a transfer of interest dissolves a partnership. (9) *In liability of members:* In absence of a special statute, a member of a corporation is not liable beyond the amount subscribed for his shares; but in a partnership, there is an individual liability of each partner to the entire extent of its debts. And, (10) *in dissolution:* A corporation can be rightly dissolved only by or with the consent of the state; partners may dissolve a partnership at any time.

EXAMPLES

1. Button acquired all the stock in a corporation and then sued Hoffman in his own name to recover possession of some personal property which had belonged to the corporation. This he could not do, but should have brought suit in the name of the corporation, as Button and the corporation were separate and distinct persons. Button vs. Hoffman, 61 Wis. 20.

2. Burral sued the Bushwick Railroad Company, a corporation, to recover certain dividends on stock owned by him, which the corporation wrongfully withheld. Objection to this suit was made on the ground that Burral was a member of the corporation and therefore could not sue it, which would have been a valid objection had the organization been a partnership. Here, however, Burral and the corporation were separate and distinct persons and the suit could be brought by Burral against the corporation. Burral vs. Bushwick Railroad Company, 75 N. Y. 211.

**358. Formation.** A corporation is created through the joint act of the state and the individuals who compose it, called the incorporators. These incorporators apply to the state for permission to organize a corporation, and upon receiving the permission of the state provide for its organization. The permission of the state may be granted either (1) by special act; or (2) by general act.

**By special act.** Until about 1840, this was the usual method of securing the permission of the state in the United States, the incorporators applying to the legislature of a state, or to Congress, for permission to form a particular corporation for a particular

purpose, the legislature or Congress then enacting a law providing that they might organize a corporation for that particular purpose and providing the powers, liabilities, and conditions under which it might exist. This special act was the charter, or franchise from the state, by virtue of which the corporation existed.

EXAMPLE

Aaron Burr secured a charter for a company to supply the city of New York with water, the legislature granting the charter by special act which further provided that the corporation should have the authority to use its surplus capital "in any way not inconsistent with the laws and constitutions of the United States and New York." The Manhattan Bank of New York City carried on its business for many years under this charter.

**By general act.** This is the usual manner in which present day corporations are created. The legislatures of the various states have passed general laws providing certain definite methods by which corporations may be organized and specifying the purposes for which they may be created and the powers which they may enjoy upon their creation. The function of the incorporators is to comply with the conditions and requirements of the general act, and make application to the officer designated therein for the issuance of a charter.

In forming corporations under general laws, strict adherence must be observed to all the preliminary requirements. The usual conditions are that the incorporators shall call a meeting, agree upon the general purposes of the corporation, provide a stock subscription, and adopt articles of association (or incorporation) which are filed usually with a county officer and also with the secretary of state, who upon payment of the statutory fee issues a certificate of incorportion. Failure to observe the conditions of the general law providing for incorporation of companies may result in the members becoming liable as partners.

**359. Property Peculiar to Corporations.** Upon the creation of a corporation it possesses certain forms of property peculiar to this form of business organization. These are: (1) The corporate charter; (2) the corporate name, and (3) the capital of the corporation.

## Corporation Charter

STATE OF ILLINOIS

DEPARTMENT OF STATE

James A. Rose — Secretary of State

**To all to whom these Presents Shall Come, Greeting:**

**Whereas,** a STATEMENT, duly signed and acknowledged, has been filed in the Office of the Secretary of State, on the _____ day of _____ A.D. 19__, for the organization of the _____ under and in accordance with the provisions of "AN ACT CONCERNING CORPORATIONS" approved April 18, 1872, and in force July 1, 1872, and all acts amendatory thereof, a copy of which statement is hereto attached;

And Whereas, a LICENSE having been issued to _____ as Commissioners to open books for subscription to the capital stock of the said Company.

And Whereas, the said Commissioners have on the _____ day of _____ A.D. 19__, filed in the office of the Secretary of State a report of their proceedings under said License, a copy of which report is hereto attached.

Now, Therefore, I, JAMES A. ROSE, Secretary of State of the State of Illinois, by virtue of the powers vested in me by law, do hereby certify that the said _____ is a legally organized Corporation under the laws of this State.

**In Testimony Whereof,** I have hereto set my hand and cause to be affixed the great Seal of State. Done at the City of Springfield this _____ day of _____ A.D. 19__ and of the Independence of the United States the one hundred and _____

SECRETARY OF STATE

*The corporate charter*, as previously defined, is the privilege granted by the state to be a corporation. This is a contract and is a form of property belonging to the corporation.

**The corporate name** is the name adopted by the incorporators of the corporation to designate this artificial person. It is required in most states that the corporate name shall include the word "company." The corporate name is property belonging to the corporation, and no other corporation in the state can use or appropriate the same name.

**The capital of the corporation** is the whole amount of its property of whatever kind. This includes the office furniture, real estate, buildings, merchandise, moneys, and the charter and goodwill of the enterprise. It may be increased through success and good management, or it may be decreased through losses incurred in the business. It represents the property of the corporation. In so far as it represents profits, it may be distributed among the stockholders in the form of dividends. Upon the dissolution of the corporation it belongs to the stockholders in proportion to their holdings of stock. It is subject to the demands of creditors of the corporation and may be seized upon execution against the corporation for its debts. Until it is distributed in the form of dividends or until the corporation is dissolved, it is the property of the corporation and not of the stockholders, and cannot be seized by personal creditors of stockholders of the corporation.

It does not include the company's capital stock, the shares of which are the property of the individual stockholders. An exception exists in the case of treasury stock, in states which permit corporations to hold treasury stock.

EXAMPLES

1. The trustee in bankruptcy of the People's Bank of Belleville petitioned the court for permission to sell the charter of the corporation as one of the assets. This right was denied, for while the charter is the property of the corporation it is not a form of property which may be sold. Fietsam vs. Hay, 122 Ill. 293.

2. The Chas. S. Higgins Company, a corporation, enjoyed a large business in manufacturing and selling soap. A rival corporation was formed which proposed to use the name of Higgins Soap Company. The use of this name by the second corporation could be prevented by an injunction, as it

was so similar to the name of the first corporation as to lead to confusion. The name of a corporation is property which it may protect. Chas. S. Higgins Company vs. Higgins Soap Company, 144 N. Y. 462.

3. The Bell Manufacturing Company owns a plant and a warehouse, has money in the bank, and has a capital stock of $10,000, the shares being owned by Ames, Bates, and Call. Dale is a creditor of the company and seeks to collect his debt by an execution. He may collect by levying upon the plant, the warehouse and the money in the bank, but he cannot seize the shares of stock owned by the members of the corporation, for these shares are their personal property, and not a part of the capital of the corporation.

### Certificate of Stock

Capital Stock
$100,000.00

1,000 Shares of
$100.00 each

**The Acme Manufacturing Company**

Stock Certificate No. 2

**This Certifies** that H. M. Miller

*is entitled to* 200 *shares of One Hundred Dollars each, in the capital stock of the Acme Manufacturing Company, fully paid and non-assessable, transferable only on the books of the Corporation by the holder hereof in person or by attorney upon surrender of this certificate properly endorsed.*

**In Witness whereof,** *the said corporation has caused this certificate to be signed by its duly authorized officers, and to be sealed with the Seal of the Corporation, at* Chicago, Ills. *this* 27th *day of* May *A. D. 19—*

SEAL

C. J. Barber
*Secretary and Treasurer*

J. E. Colby
*President*

### Assignment of Stock Certificate

**For Value Received,** *I hereby sell, assign and transfer unto Jennie Baldwin Edgewater, of Chicago, twenty shares of the capital stock represented by the within certificate, and do hereby irrevocably constitute and appoint Henry Appleby my attorney to transfer the said stock on the books of the within-named Company, with full power of subscription in the premises.*

*HENRY FALWORTHY.*

*Dated August* 9, 1916, *in the presence of*
*WALTER S. WHEELER.*

**360. Capital Stock.** By means of a capital stock divided among the members of the corporation it is possible to distribute the authority of managing the corporation and receiving its dividends among a number of persons. There is much confusion in the use of the terms *capital* and *capital stock* as applied to

corporations. The capital of a corporation is, as defined in the preceding section, the whole amount of its property of whatever kind. The capital stock is the amount which it has obtained, or is authorized to obtain, from its members by way of subscription. The capital stock is a sum fixed by the corporate charter as the amount paid in or to be paid in by the subscribers for the conduct of the business of the corporation. The stock is represented by certificates, called stock certificates, or shares of stock, which entitle the holder to share in the management, profits, and assets when distributed, of the corporation to the extent which his stock bears in proportionate to the total capital stock of the corporation.

By their subscriptions to the capital stock, the subscribers agree that they will pay for the stock subscribed by them as calls are made. A stockholder who receives his original stock at a discount is liable upon the demand of creditors of the corporation for an assessment for the difference between the purchase price and the par value of the stock bought. It is not, however, required that stock shall always be paid for in money; it may be issued in exchange for property or services. If the property or services fairly represent the par value of the stock issued in exchange therefor, there is no further liability as to creditors. This is regulated by statute in some states.

EXAMPLE

The Dove Company, a corporation, is created with a capital stock of $30,000 distributed among Black, Jones, and Young, who each pay one-third of this amount to the company and receive stock certificates, Young paying his share by contributing his inventions, which it is agreed shall be valued at $10,000. The capital stock of the corporation is $30,000, but the capital at the beginning of the enterprise is $20,000 in cash and the inventions of Young, an entirely different thing from the capital stock.

The money which the shareholder pays for his stock becomes a part of the capital of the corporation. It may be invested in machinery, land, or merchandise, and may increase or decrease in amount and value, depending upon the success or failure of the business.

Each corporation, except a few special forms of charitable and religious corporations known as non-stock companies (or cor-

porations not for profit) has a specified capital stock. When corporations are formed under general laws, provision for the amount of capital stock is made in the articles of association and in the application for a certificate of incorporation. The actual capital of the company may vary materially from year to year, but the capital stock can be changed only by amendment of the articles of association with the permission of the state, or by further compliance with the general law regarding corporations.

**361. Membership in Corporations.** Membership in a stock corporation consists simply in the ownership of one or more shares of stock. Stock may be acquired either by (1) subscription, or (2) by transfer from a prior holder, either by purchase or as a gift.

The contract between the corporation and a third person by which the third person agrees to contribute a certain amount of money or property to the business of the corporation in return for the issuance to him of stock certificates is called the subscription. It is usual to secure a number of such contracts before the formation of the corporation is completed, and some states require that certain proportions of the total capital stock shall be subscribed and other proportions paid for in cash, or its equivalent, before the corporation may be created.

After shares of stock are issued they are personal property which may be sold or transferred by gift from one person to another. Some formalities must be observed in the transfer of shares of stock, however, that are not required for the transfer of other personal property. It is usual to transfer a stock certificate by an assignment of the interest of the holder to the purchaser, the assignment usually being written upon the back of the certificate. The new holder then secures a registry of the transfer on the books of the company, which registry serves as notice to the corporation that he is now the holder of the stock and entitled to the rights of the shareholder. It is customary and in some corporations compulsory for the new holder to deliver up the old stock certificate to the corporation, which issues a new certificate naming him as the stockholder. The corporation would be protected if it paid a dividend to an original holder in

good faith without notice of the transfer of the stock, and the new holder's only remedy would be against the prior holder of the stock who had wrongfully received the dividend. Similarly, creditors are entitled to assume that the person named on the books of the company is the owner of the stock and may levy upon a declared dividend as his property.

EXAMPLE

Brydon owned 488 shares in the North Branch Company. He sold and assigned a part of this stock to Gemmell, who gave notice to the company and demanded that his stock be registered and that he be paid all future dividends. The officers of the corporation refused to register his shares. He was entitled to bring suit against them for dividends which they paid to Brydon, as he had given them notice of his ownership in the stock and any future payment to Brydon was not in good faith. The officers had no right to refuse to register his stock. Gemmell vs. Davis, 75 Md. 546.

**362. Classes of Stock.** The capital stock of a corporation may be of two kinds: (1) common, and (2) preferred. *Common stock* is stock the owners of which are not in any way specially preferred or favored. The owner of common stock is entitled to one vote in the management of the corporation, for every share he owns. He shares in the common stock dividends (and in case of the dissolution of the corporation, in the assets) in proportion to the amount of stock he owns. In the absence of special provisions all stock is common stock.

**Preferred stock** is stock which entitles the owner to receive dividends, or to share in the distribution of corporate assets, or both, before or in preference to the holders of common stock. Preferred stock can be issued only when the corporation has the special power to issue it, and the preferred stock certificate usually states that the holder shall be entitled to a certain specified dividend on his investment which shall be paid out of the profits of the company before any payment of dividends shall be made to holders of common stock. In some corporations the preferred stock shares equally with the common in the dividends remaining after the preferred dividends have been paid, but as a general rule the preferred stock is limited to a fixed amount, after which all dividends accrue to the benefit of the holders of common stock. Thus the common stock frequently receives larger dividends than the preferred.

# Articles of Incorporation
of
# Buffalo Hill Mining and Development Company

## Know All Men by These Presents:

*That we, the undersigned, George N. Wright, James A. Lyons, and John E. Evans, for ourselves, our associates and successors, have associated ourselves together for the purpose of forming a corporation under and by virtue of the statutes and laws of the State of South Dakota, and we do hereby certify and declare as follows, viz.:*

1. *That the name of this corporation shall be "Buffalo Hill Mining and Development Company."*

2. *That the purpose for which this corporation is formed is to conduct the business of:* (a) *Mining, smelting, refining, reducing, and dealing in and with all sorts of ores, metals, and minerals, and the prospecting, locating, opening, operation, and developing of mines, oil wells, quarries, and mineral deposits of all descriptions;* (b) *Constructing and operating mills, factories, machine shops, and industrial plants of all descriptions, and the buying, selling, and dealing in and with all supplies, merchandise, and materials, raw and prepared, useful or convenient, in connection therewith.*

3. *The place where the principal business of this corporation shall be transacted is Pierre, in the County of Hughes and State of South Dakota.*

4. *The term for which this corporation shall exist shall be twenty years.*

5. *The number of directors of this corporation shall be three, and the names and residences of such, who are to serve until the election of their successors, are as follows:*

| *Names:* | *Residences:* |
|---|---|
| *George N. Wright* | *Chicago, Ill.* |
| *James A. Lyons* | *Huron, S. Dak.* |
| *John E. Evans* | *Mitchell, S. Dak.* |

6. *The amount of the Capital Stock of this corporation shall be and is Two Hundred Thousand Dollars, divided into two thousand shares of the par value of* $100 *each.*

**In Testimony Whereof,** *we have hereunto set our hands this 29th day of September,* 1916.

[Signed] *GEORGE F. WRIGHT.*
*JAMES A. LYONS.*
*JOHN E. EVANS.*

## Stock Subscription

**Subscription List**

### The Everready Manufacturing Company

**To be Incorporated under the Laws of New York**

*Capital Stock*, $50,000

*Shares*, $100 *each*

*We, the undersigned, hereby severally subscribe for and agree to take at its par value the number of shares of the capital stock of The Everready Manufacturing Company set opposite our respective names, and agree to pay therefor in cash on demand of the treasurer as soon as said company is organized.*

*Albany, New York, February* 24, 1916.

| *Names* | *Addresses* | *Shares* | *Amount* |
|---|---|---|---|
| *Gordon Ambrose* | *Suffern, N. Y.* | 10 | $1000 |
| *H. C. Mackey* | *Albany, N. Y.* | 5 | 500 |

## REVIEW QUESTIONS

1. Henry Ames, a brother of George Ames, desires the latter to assist him in financing a manufacturing business, suggesting that they form a partnership. George Ames is a wealthy man, while Henry Ames has been unsuccessful many times in business, but apparently has a valuable proposition this time. What advice would you give George Ames regarding the kind of business organization which should be formed? Why?

2. Samuels has loaned $5000 to Johnson and seeks to collect payment. He secures a judgment against Johnson. He learns that Johnson owns thirty shares of stock, valued at $100 a share, in the Acme Manufacturing Company, a corporation. This is one-third of all the capital stock of the company, which has assets of $20,000, having been a profitable undertaking. How may Samuels collect his claim? Why?

3. Ames and Bates acquire all the stock in the Cool Dairy Company, a corporation, and desiring to sell the real estate belonging to the company, execute a deed in their own names as the owners of the property to Dale. Does Dale secure a title to the property? Why? Would he have done so if the Cool Dairy Company had been a partnership between Ames and Bates? Why?

4. The A corporation receives a charter from the state empowering it to build a toll-bridge across a river and to charge a fee for travel, the charter providing that this corporation shall have the exclusive right to maintain a toll-bridge within one mile of that place for thirty years. Two years later the state grants another charter to the B company empowering it to operate a steam ferry within a hundred yards of the bridge. This cuts the revenue of the A corporation in half. Has the A corporation any remedy? Why?

## CORPORATIONS — Continued

- Powers
  - 1. Express
  - 2. Implied
    - a. To buy and sell land
    - b. To acquire property by will
    - c. To borrow
    - d. To issue notes
    - e. To pledge its property
    - f. To make by-laws
    - g. To use a seal

**363. Powers of a Corporation.** Upon its organization a corporation possesses the power to act in accordance with the provisions of its charter. In addition it has certain implied powers. Among these are: (1) Power to acquire land, necessary for the business of the corporation, by purchase; (2) power to sell and transfer the title to land; (3) power to acquire property by will from another; (4) power to borrow and issue negotiable instruments; (5) power to mortgage or pledge its property; and (6) power to make by-laws, rules, and regulations for the conduct of its business; (7) power to use a seal.

These express charter powers and the powers implied from the creation of the corporation are exercised by the stockholders, acting through officers elected by them, called the *board of directors*. The stockholders may be very numerous and too large and unwieldy a body to assume personally the active management of the corporation. They control the corporation, therefore, only through the medium of the board of directors. These directors are elected at the annual meeting of the stockholders, and as they represent the will of the holders of the majority of the stock, it is said that the control of the corporation is in the hands of the holders of the majority of the stock, whose power is absolute so long as they act within the provisions of the charter and the implied powers of the corporation.

**364. Directors—Powers and Duties.** The powers of the directors are very extensive and are fixed by the charter. While the control of the corporation is in the hands of the majority of the stockholders, the active management of the corporation is in the hands of the directors. When assembled as a board, they are the embodiment of all the corporate powers, except those exercised by the stockholders. They could not engage the capital of the corporation in an unauthorized enterprise, nor could they increase or decrease the capital stock, dissolve the corporation, or consolidate it with another corporation, for these are powers vested in the stockholders and many of them cannot be exercised even by them without the unanimous consent of all the stockholders together with the consent of the state. But in the active business management of the corporation within its express and implied powers, the directors are supreme.

The position of the directors is virtually that of business agents of the majority of the stockholders. They are bound to exercise reasonable care in the management of the corporate business, and are liable for losses resulting from their carelessness and neglect. They cannot be held liable for losses occasioned by bad business judgment if they have acted in good faith. Being agents, they cannot make a secret profit in transacting the corporate business, nor secure to themselves any personal advantage at the expense of the stockholders.

**365. Officers and Agents.** The board of directors usually elects the officers of the corporation in accordance with the provisions of the by-laws of the corporation. These officers are usually the president, vice-president, secretary, and treasurer. Sometimes there is a business manager. The president is usually also the chairman of the board of directors. His duties are provided by the by-laws of the corporation, and when no business or general manager is elected he is the active business head of the corporation. As the chief officer of the corporation, he is generally empowered to execute deeds, negotiable instruments, and other documents, in the name of the corporation.

The duties of the vice-president, secretary, treasurer, and business manager if any, are the usual duties falling to such

officers. Their acts are binding upon the corporation if within the scope of their general authority.

Other officers and agents are sometimes appointed in accordance with provisions of the by-laws. These officers and agents are authorized to act in certain matters only, and they are answerable to the corporation in the same manner that an ordinary agent would be answerable to his principal. They may bind the corporation when acting within the scope of their special authority, and are liable for their negligence.

**366. Rights of Stockholders.** In addition to the right of the majority of the stockholders to control the corporation within the scope of its charter powers, the individual stockholders have certain rights which cannot be taken from them. They have the right to inspect the books and records of the corporation, and to inquire at all reasonable times into the affairs of the corporation. They may request the corporation to sue a director believed to be guilty of a breach of duty, and if the corporation fails to act may themselves sue in the name of the corporation, and similarly may prevent the officers or directors of the corporation from engaging in unlawful enterprises or from performing unwarranted acts, and dissipating the resources of the corporation. They have the right to receive dividends after they have been declared. They are entitled to be notified of all meetings of stockholders, to attend all meetings and participate in them by voting on all matters. In some states by statute they are allowed to vote by proxy. They have the right to transfer their shares. Upon the dissolution of the corporation, those who hold stock at that time have the right to participate in the division of the corporate assets.

**367. Liabilities of Stockholders.** One advantage that has tended to popularize corporations more than any other is that in general the stockholders are not personally liable for the corporate debts, beyond the amount of their unpaid stock subscriptions. If the corporation should become insolvent, the stockholders may lose their investment in the stock, but if their stock is fully paid for they cannot be called upon to pay any part of the corporate debts from their private fortunes. They are, however, liable to creditors to any amount which may be unpaid

on their stock subscriptions. The creditors are entitled to rely on the supposition that the stockholders have paid for their stock at its face value, and have contributed to the capital and assets of the corporation in the amount which their stock certificates would indicate. If the stock has been issued without full payment the creditors may compel the stockholders to pay for it. For this reason it is dangerous to buy stock that is sold at less than par.

In many states there are special statutes providing that the stockholders in banking corporations are liable for an additional amount equal to the par value of their holdings. Holders of National Bank stock always have this liability. A few states have applied this rule of "double liability" to all corporations.

If a stockholder has received a division of the assets of the corporation at a time when the corporation owed creditors which it could not pay, he must return the amount which he received for the benefit of the creditors. It would be extremely unfair to allow a corporation in failing circumstances to divide the capital among the stockholders and leave the creditors without assets from which to collect their debts.

EXAMPLE

A corporation was organized with a capital stock of $100,000, only seventy-five per cent of the stock being subscribed for, and the remaining twenty-five per cent being given to the purchasers of the stock as a bonus. Later the corporation became insolvent, and the creditors were permitted to compel the stockholders to pay in full for unpaid portions of their subscriptions, and for the stock issued as a bonus. Fogg vs. Blair, 133 U. S. 534; Hosper vs. Car Co., 48 Minn. 174.

**368. Rights of Creditors.** As previously stated, the creditors of a corporation are entitled (1) to assume that the amount of capital purported to be invested in the corporation is in fact so invested and fully paid up; and (2) to be paid out of the assets of the corporation upon its insolvency before its distribution among the stockholders. A further right of creditors is to protect their claims against fraudulent acts which will cause irreparable injury to their security, but creditors cannot object to acts of the stockholders which are outside the scope of their charter powers so long as they are not fraudulent, or do not make the corporation insolvent.

**369. Unauthorized Acts.** Acts which are not authorized by the charter are called *ultra vires* acts, the term meaning beyond the lawful power and authority of the corporation. When the majority of the stockholders of a corporation seek to perform an *ultra vires* act they are in reality violating the two contracts which the corporation represents, the contract between the state and the corporation and the contract between the stockholders, both providing that the corporation shall act only within its charter powers, express or implied. Consequently, any stockholder who discovers that the corporation is acting, or is about to act, through its directors, representing the majority of the stockholders, in such a way as to hazard the property of the corporation in unauthorized undertakings, may bring a suit to restrain such action. The state may also protect itself against the violation of the contract represented by the charter, and prevent usurpation of powers, by bringing a suit to dissolve the corporation and terminate its charter.

**370. Defective Organization.** Sometimes the incorporators fail to comply strictly with the general incorporating act, but nevertheless proceed to act as if they had created a corporation. Such an organization has not a valid, legal existence as a corporation, but is known as a *de facto* corporation. The failure to comply with the necessary requirements of organization has prevented it from being a true corporation. To constitute a *de facto* corporation three things must be shown: (1) A charter or general incorporation law; (2) an unsuccessful attempt to organize a corporation under the law; and (3) a use of the rights claimed to be conferred by it. When these three elements are present, and the incorporators have attempted to form a corporation, and despite their failure, have acted as though they were a corporation, only two classes of people can object to their acting as a corporation. These are the state, which may commence legal proceedings, known as ouster proceedings to prevent a further use of the powers, and stock subscribers, who may refuse to pay for their stock until a true and valid corporation is created. The rights of creditors and others who deal with the organization as a corporation are the same as though a true corporation had been created, except in a few states, most

notably Illinois, where it has been decided that the members of a *de facto* corporation are liable to creditors as partners; that is, they cannot claim the benefit of limited liability.

EXAMPLE

An effort was made to incorporate under a state law requiring the certificate of incorporation to be subscribed and acknowledged by five members, and recorded in the county in which its principal office was located. Only four members signed the certificate, and the state brought suit to prevent the corporation from transacting business. The court granted the state the relief requested. People vs. Water Company, 97 Cal. 276.

**371. Dissolution of Corporation.** A corporation may be dissolved: (1) By expiration of the time mentioned in the charter; (2) by a surrender of the charter, accepted by the state, or made in accordance with the provision of the general act; (3) by forfeiture of the corporate charter, through a proceeding in the courts for that purpose, because of non-use or mis-use of the charter and powers granted; or (4) by repeal of the corporate charter by the legislature, in states where the power to repeal such charter is reserved to the state in the state constitution.

Upon the expiration of the time for which a corporation was created it is dissolved automatically. It can no longer transact business except such as is necessary to wind up its affairs. Methods are usually provided by which a certain proportion of the stockholders may vote to close up the affairs of the corporation, dissolve it, and divide its capital after payment of creditors. The statute must be carefully followed to effect a valid dissolution. The state is at all times empowered to forfeit the charters of corporations which have mis-used their powers, or to prevent corporations from continuing in business when their creation was defective. Not only may the state do this, but in nearly all of the states there are constitutional provisions declaring that the power to repeal, alter, and amend corporate charters is reserved to the legislature and cannot be granted away. Hence, although the charter is a contract between the state and the corporation, this reserved power of the state enables future legislatures to enact many corporate laws which would otherwise be forbidden.

**372. Liquidation of Assets.** The management of the dissolving corporation is placed in the hands of a liquidating

officer. His duties are to collect all the corporate assets, reduce them to money if possible, pay off creditors, and distribute the balance proportionately among the stockholders. The right of creditors to the assets of a defunct corporation are primary, and the rights of the stockholders secondary.

**373. Foreign Corporations.** One state cannot authorize a corporation to transact business in any other state, but by the reciprocal courtesy and good-will of states, the right of a corporation chartered by one state to do business in another is quite generally recognized. This privilege, however, is subject to many restrictions, and conditions are frequently imposed upon these corporations, called "foreign" corporations, with which they must comply before engaging in business in a state in which they were not chartered. Among the usual conditions are that the corporation shall file with the state in which it proposes to do business a copy of its charter, a statement of its financial resources, and a list of its officers.

## REVIEW QUESTIONS

1. Malone, a minority stockholder in the Morris Service Company, a corporation, discovers that the directors have unanimously agreed to engage the funds of the corporation in booming a tract of land owned by them for their personal benefit. The directors are also the majority stockholders, but the act in which they are engaged is beyond the corporate powers. May Malone sue them in the name of the corporation without any further act on his own part? Why?

2. The Belden Machine Company, a corporation authorized to engage in manufacturing and trading, invests its money in a banking enterprise. What persons, if any, may object? How? Why?

3. Several men meet and attempt, in good faith, to organize a corporation under a general act of the legislature. They fail to conform to a certain provision of the law with which they are unfamiliar, but proceed to act and transact business as a corporation. Lawson, who has subscribed for twenty shares of stock in the corporation, on discovering this fact, refuses to pay for it; and Wilson, who has contracted to build an office for the corporation, refuses to perform his contract. Has the organization any rights against Lawson? Against Wilson? Why?

4. The directors of the Congress Hotel Company, a corporation, spent large sums of money in improving the dining room service, hiring orchestras and employing entertainers. The dining room had never been a revenue-

producing part of the establishment, and continued to lose money, the company eventually becoming insolvent by reason of the expenditures of the directors. They had hoped to attract patronage from rival hotels in the city, but it was generally admitted that their course had been an unwise business policy. May the directors be held liable for the loss? Why? To whom?

## PRACTICAL SUGGESTIONS

In a corporation:

I. As a stockholder you are subject to no financial liability, except in case of a banking corporation, beyond the amount still to be paid on your subscription. A creditor of a corporation can satisfy his claim out of the assets of the corporation only.

II. A stockholder is not an agent to bind the corporation by his acts unless he has special authority.

III. A corporation is not dissolved by the death, insanity, or bankruptcy, of a stockholder.

IV. A stockholder may sell his stock without working a dissolution of the corporation.

V. The holders of the majority of the stock have the right to manage the business of the corporation so long as they remain within the powers contained in the charter.

VI. You have no voice in the corporate management within the charter limits beyond the power to vote in proportion to your stock holdings, unless you are an officer.

## CHAPTER XLII

## JOINT STOCK COMPANIES

**374. A Joint Stock Company** is a company that is similar, in business organization, to a corporation, but is in reality a partnership with a large number of members.

The joint stock company is a form of business organization so little used that it would not be necessary to treat it were it not for the fact that many persons confuse joint stock companies with corporations, and it is important that the distinction between the two be fully understood.

**375. The organization** of a joint stock company is similar to that of a corporation in that stockholders' meetings are held, a board of directors is elected, and business is transacted by officers selected by the directors. The interests of the various members of the company are represented by shares of stock, as in a corporation, and the profits of the business are distributed in the form of dividends.

**376. Liability of Members.** The resemblance to a corporation is in the form of organization as described above, and ends there. The members of a joint stock company are partners, and as a partner each is liable for all of the debts of the company.

**377. Compared with Partnerships.** As above stated, joint stock companies are like partnerships in the liability of members. They also resemble partnerships in that their formation requires no special state authority, but simply the agreement of those who thereby become members. Like a partnership, a joint stock company must sue or be sued in the names of its members, and not in the name of the company.

**378. Compared with Corporations.** It has been shown that in their organization and manner of doing business, joint stock companies are like corporations. They also resemble corporations in having the "power of succession"— they are not automatically dissolved upon the death of a member. They are

dissolved by lapse of the time for which they were organized, or by decree of court. They cannot be dissolved at the demand of a member.

Stock companies being similar in organization to corporations, it sometimes happens that ineffectual attempts to create a corporation result in the formation of a stock company, if the company goes ahead and transacts business without its charter. If a corporation continues in business after its charter has expired, without renewal, it continues as a stock company.

The corporation is the outgrowth of the joint stock company. Though the two are organized and managed in the same way, the promoters of new organizations of the kind usually seek corporate charters, because of the freedom from personal liability enjoyed by the stockholders in a corporation. This is the principal reason for the practical disappearance of the joint stock company.

## CHAPTER XLIII

## INSURANCE

**379. Introduction.** Insurance is a form of contract by which one party, in consideration of a sum of money, agrees to reimburse another party in the event of the loss of, or injury to, or death of, the subject matter specified in the contract. The party assuming the risk is called the *insurer:* the other party to the contract is called the *insured.* Since insurance is a contract, the ordinary rules of the law of contracts are applicable to it.

The theory of insurance is that while a loss might overwhelm an individual, if the same loss is distributed among many, it can be borne without serious inconvenience to any one of them. The manner in which the loss is borne by the many is by their making relatively small periodical payments to create a fund from which any loss is paid when it occurs. Insurance is an economic necessity and performs an important function in commercial transactions.

**380. Policies and Premiums.** The contract by which the insurer agrees to compensate the insured in case of loss of the nature specified in it is called an *insurance policy.* The maximum amount which the insurer will pay in case of loss is called the *face of the policy.* The amount which the insured must pay for complete or partial indemnity in case of loss is called the *premium.* This premium, together with other premiums received from similar insurance policies, is used to form a fund sufficient to pay indemnities as required. The insurer ordinarily derives his profit from the business by using this fund and receiving interest for its use.

**381. Kinds of Insurance.** The principal kinds of insurance are: (1) Fire; (2) life; (3) marine; and (4) casualty.

**Fire insurance** is a contract by which the insurer agrees to indemnify the insured against loss by fire.

**Life insurance** is a contract to pay a designated person a sum of money in the event of the death of the person whose life is insured.

**Marine insurance** is a contract to indemnify the insured against loss of property in ships and their cargoes by the perils of the sea.

**Casualty insurance** is a contract to indemnify the insured against accidental injury, some policies insuring the person and others insuring property.

## FIRE INSURANCE

**382. Form of Policy.** The contract of fire insurance specifies: (1) The insurer; (2) the insured; (3) the property insured; (4) the conditions under which the insurer will bear the loss, if any; (5) the term and premium of the policy, and (6) a maximum amount beyond which the insurer will not be responsible for loss.

Contracts of insurance containing the last mentioned specification are designated as *open policies*, and are the customary form of fire insurance. In the event of loss suffered under such a policy the insured must make claim showing the amount of damage actually suffered. If this be less than the total amount of the policy, he can only recover for the actual loss suffered. In no event can he recover beyond the maximum amount specified in the policy. This form of policy is distinguished from a *valued policy* in which the value of the property to be insured is conclusively agreed to by the parties and in the event of loss no question is raised as to the amount of the damage, but solely as to whether the loss which the policy covered occurred. The valued policy is occasionally used in fire insurance, but is generally confined to life and marine policies.

In many states the form of policies of fire insurance has been regulated by statute, the New York Standard form of policy being popular at present. Other states have made some variations in the form of policy required, but in general the New York form has been adopted as the standard fire insurance policy.

**383. Who May Be Insurer.** At common law any person could become an insurer, but the exercise of this right is now quite generally limited in practice to corporations created and existing under special laws relating to insurance companies, and as the business of these companies is public in its nature, they are controlled and regulated for the protection of the public. In addition to the regular insurance companies, doing business for a profit, there are several so-called fraternal orders or mutual benefit companies, which instead of attempting to make a profit by the accumulation and use of premiums, aim to distribute the losses as they occur in the form of annual assessments among the members.

**384. Who May Be Insured.** The fire insurance policy being a contract, it is essential that the parties shall have capacity to contract. If a person under legal or physical disability enters into a contract of fire insurance the contract is voidable at his option like any other contract.

Not only do the ordinary requirements of contracts apply to fire insurance policies, but in addition the insured must possess what is known as an *insurable interest* in the property insured.

**385. Insurable Interest.** A person is said to have an insurable interest in property when he is so situated in reference to it that by its destruction he will suffer an actual loss of money or legal right, or incur a legal liability. If this insurable interest were not required to be present, an insurance policy would be a mere wager in which one person would virtually be wagering a small amount of money against a larger sum that a contingent event would happen. The insured could purchase a policy by payment of the premium on property which he did not own, and would be in a position to receive a specified amount in the event of its destruction. He would have no interest in its preservation, but would be concerned only with its demolition, and to permit the creation of such contracts would be antagonistic to public policy. If, however, the insured has an insurable interest in the thing insured, there is not so great a temptation on his part to destroy it for the purpose of recovering the insurance, and the contract is deemed valid in law. The doctrine requiring the presence of this insurable interest in the property insured is a reasonable one.

It is not necessary that the insured shall actually own the property insured, provided he possesses a valuable interest in it. He must possess some property interest, not purely speculative, but real, which is of such a nature as to make him concerned with its preservation.

EXAMPLE

A stockholder in the Merchants' Steamship Company, a corporation, purchased a policy of insurance on property belonging to the corporation, paying the premium. Upon the destruction of the property he sued the insurance company for the amount of his loss and was allowed to recover, his insurable interest in the property being found in the fact that as a stockholder in the company he was interested in the preservation of its property so that profits might be distributed in the form of dividends. Riggs vs. Insurance Company, 125 N. Y. 7.

**386. Representations.** A written application is often required for a fire insurance policy. A statement made in this application, or one made orally at the time of applying for the insurance, is called a representation. If a representation is material and is made falsely or fraudulently the policy will be void, for the insurer has a right to inquire into the circumstances of the risk which he is assuming and to rely on answers to his questions. It is presumed that the insurer will request information on all material points and that the insured is not bound to advance information except in answer to questions. The concealment of facts will not ordinarily render a fire insurance policy void unless it clearly appears that the concealment was a part of a general scheme to defraud the insurer.

EXAMPLE

The following question: "For what purpose is the building occupied and by whom?" was answered, "By the applicant; for the manufacture of lead pipe only," while as a matter of fact the building was also used to manufacture reels on which to wind the lead pipe. This was not a misrepresentation, however, for it was immaterial and was reasonably included in the general business of manufacturing lead pipe. Collins vs. Insurance Company, 10 Gray (Mass.) 155.

**387. Warranties** are express promises or undertakings by the insured which are made a part of the policy. They differ from representations which are statements made preliminary to the contract of insurance and are merely inducements for entering

into it and which are not written into the policy. Being included as terms in the policy of insurance, warranties have the effect of conditions precedent to liability under the contract and the contract may be avoided if they are not fully performed. A representation need only be substantially correct, and it avoids the policy only if false on so material a point that it actually induced the company to enter into the contract. On the other hand, a warranty must be exactly performed, and its materiality cannot be questioned, since the parties have made it one of the conditions of the contract.

Among the usual warranties included in fire insurance policies are clauses prohibiting an increase in the hazard of the risk by changes in the subject matter, prohibiting a change of ownership, the keeping or using of dangerous articles on the premises, the permitting of the premises to become vacant and unoccupied for more than a limited period of time, and the taking out of insurance in furtherance of an illegal act.

EXAMPLES

1. An insurance policy, containing a clause that it did not insure property used in an illegal business, was taken out to cover a stock of liquor exposed for sale in territory where the sale of liquor was prohibited by law. Upon the destruction of the stock of liquor no recovery was allowed against the insurance company. Kelly vs. Insurance Company, 97 Mass. 288.

2. A saw-mill was insured, the policy containing the usual clause prohibiting vacancy for more than ten days. Because of the breaking of a saw and the low stage of water, the mill was not used for more than ten days, although all the machinery remained and there was lumber to be sawed as soon as there was sufficient power. The court decided that the clause against vacancy and unoccupancy had not been broken. Whitney vs. Insurance Company, 72 N. Y. 117.

3. The owner of a house moved out for six months, leaving only a few pieces of furniture and occasionally sleeping there. This amounted to a vacation of the house, the attempted use being insufficient to keep the insurance alive. Insurance Company vs. Hamilton, 82 Md. 88.

**388. Assignment of Policies.** The New York Standard form of fire insurance policy and most other policies specifically require the consent of the insurance company to an assignment of the policy. This is in accordance with the general policy of the law to hold insurance contracts non-assignable without the consent

of the insurer, and void if assigned without the consent of the insurer. If the insurer consents to an assignment there is virtually a new contract formed between the insurer and the person to whom the contract is assigned. After an assignment with consent the policy will be unaffected by any future act of the original holder.

EXAMPLE

Smith owned certain property, insured it, sold it to Brown, and assigned the insurance policy to Brown with the consent of the insurance company. Brown then mortgaged back the property to Smith, and reassigned the policy to Smith without the consent of the company. Later Brown committed an act which violated the policy. Upon the destruction of the building by fire, Smith sued on the policy but was refused recovery, the company not having consented to the second assignment, and the act of Brown being a violation of which the company could take advantage. Smith vs. Insurance Company, 120 Mass. 90.

**389. Proof and Recovery of Loss.** It is generally provided in the insurance policy that notice of loss must be given immediately to the company, and that proofs of the nature and amount of loss must be presented to the company within a limited period, usually sixty days.

EXAMPLES

1. After the great Chicago fire in 1871 notice of the loss by fire was not given to the company until five weeks after the fire. This was considered to be an "immediate notice of loss" under the peculiar circumstances, on account of the resulting general confusion at that time. Insurance Company vs. McGinnis, 87 Ill. 70; Insurance Company vs. Gould, 80 Ill. 388.

2. A delay of forty-eight hours in giving notice of the loss was a failure to comply with the provision requiring "immediate" notice, where there was no good reason for the delay. Brown vs. Insurance Company, 40 Hun. (N. Y.) 101.

3. A fire continued for several days and within sixty days after it was extinguished, but more than sixty days after it originated, proofs of loss were made to the company which had insured the building. This was a compliance with the provision requiring that proofs of loss be made within sixty days, as the time does not begin to elapse under this provision until the fire is extinguished and the ruins sufficiently cooled to permit an examination of the loss. Wall Paper Company vs. Insurance Company, 175 N. Y. 226.

The policy usually insures against "all direct loss or damage by fire." *Fire* is defined to mean combustion plus light and heat, and destruction by chemicals so as to leave a charred surface,

but damage when there has been no flame is not a loss covered by a fire insurance policy. Similarly, damage caused by lightning without a resulting combustion is not a loss by fire. The policy also covers only *hostile* fires as distinguished from *friendly* fires, a friendly fire being one which was intended by the insured, but which incidentally produces certain unintended losses. These losses are not recoverable under a fire insurance policy. A fire may, however, originate as a friendly fire and get beyond control so as to become a hostile fire in which event any loss will be recoverable from the insurance company.

There can be no recovery from the insurer if the damage by fire is intentional on the part of the insured, but the insurer cannot refuse payment for losses on the grounds that the fire was caused by the carelessness of the insured.

EXAMPLES

1. A flue in the drying room of a sugar refinery was left closed one night and the following morning the sugar was found to be ruined by smoke from the heating plant. No recovery was allowed as the only fire in the place was the one in the heating plant which had been intended. Austin vs. Drewe, 6 Taunt. (Eng.) 436.

2. Way built a fire in the stove to burn some papers, and the soot in the chimney became ignited and damaged the chimney. This loss was recoverable for the fire had become a hostile fire. Way vs. Insurance Company, 166 Mass. 67.

The insurer is liable for losses which (1) follow directly from a hostile fire without intervening cause, and (2) which, although not directly following from the fire, are the natural consequences from it which result in the ordinary sequence of events.

EXAMPLE

Damages resulting to goods while they were being removed from threatened injury by fire, were promptly chargeable to the insurance company. White vs. Insurance Company, 57 Me. 91.

**390. Special Right of Insurer Paying Loss.** Upon the payment of a fire loss the insurer acquires whatever rights the insured had, to have recovery against third persons for the loss. The insurer is said to be *subrogated* to the rights of the insured. Thus when one's house has been destroyed by a fire originating from the negligence of a third person, the owner may recover for his

loss either from the insurance company or from the person starting the fire. He cannot do both. If he recovers from the insurance company, the company then acquires the right to recover from the third person. If the owner should first recover damages from the third person and thereafter collect for the loss from the insurance company, the latter could, upon discovering the facts, recover from the owner the amount paid on the policy.

**391. Double Insurance.** In the event that the insured holds policies from a number of companies, he could in the absence of statute or special provisions in the policy collect his loss from any one of the companies, provided it did not exceed the maximum of that particular policy. That company in turn could recover a *pro rata* share from each of the other companies. To avoid this circuitous procedure, it is customary for policies to provide that the company shall be liable for only that proportion of the loss which the amount of its policy bears to the total amount of insurance.

## REVIEW QUESTIONS

1. Armour applied for an insurance policy and in answer to a question on on the application blank as to the amount of insurance on his building stated that he had $10,000. The company issued him a policy for $3000, relying on this statement, but would have refused to do so had he carried a smaller amount of other insurance. As a matter of fact all his other insurance had expired, though he did not know it. Could the insurance company avoid its policy for $3000? Why?

2. Peyson insured his home for $5000. His wife left shortly afterwards to visit her parents and was absent for eight months. The furniture remained in the house and Peyson, who was a commercial traveler, slept in the house whenever he was in the city, which was frequently. A fire destroyed the house. The insurance policy contained a clause providing that the policy was void if the premises were vacant and unoccupied for more than ten days. Could Peyson recover for his loss? Why?

3. Jenkins took out an insurance policy on his home. He sold the house to Smith and, with the consent of the insurance company, assigned the policy to Smith. The policy provided that no gasoline should be used on the premises with the consent of the owner. After the sale and assignment of the policy, Jenkins ordered a barrel of gasoline delivered to his house, and the deliveryman, not knowing of his removal, delivered the gasoline to the house occupied by Smith. Before Smith discovered the gasoline, it ignited by

spontaneous combustion and started a fire which destroyed the house. May Smith recover from the insurance company? Why?

4. Johnson had taken out insurance on his barn. In order to drive out wasps he lighted a wisp of hay and thrust it into the dry timbers of the barn. Other hay in the vicinity was ignited and the barn destroyed. May Johnson recover for his loss from the insurance company? Why?

5. Murphy insured his store building and its contents against loss by fire. A fire occurred which caused the following items of damage: $3000 by destruction of merchandise; $2000 by injury to the building; $500 by injury to goods from water in attempting to check the fire; $200 by goods stolen while being removed from the building; and $400 for medical services and nursing occasioned by his falling from a ladder while attempting to remove the goods. The policy stated a maximum of $15,000. For what losses may Murphy recover? Why?

## CHAPTER XLIV

### INSURANCE — Continued

#### LIFE INSURANCE

**392. Form of Policy.** Life insurance, being conditioned for the payment of a definite sum upon the happening of a particular event — the death of the person whose life is insured — requires a valued policy. It is immaterial whether the death of the person has occasioned a loss in a greater or less sum to the person to whom payment is to be made, for the valuation stated in the policy itself is the controlling factor.

**393. The Types of Valued Policies** which predominate in life insurance are: (1) Straight life, (2) limited payment life, and (3) endowment policies. The first two types are similar in that the insurance company contracts to collect a stated annual or semi-annual premium and to pay a definite sum to a designated person upon the death of the person whose life is insured. These two types differ only in the fact that under a straight life policy these payments continue until death, while under a limited payment life policy it is provided that the payment of premiums shall cease after a specified period, usually ten, twenty, or thirty years.

The purpose of these policies is the protection of those dependent upon that person. These policies have given rise to the popular statement that "in life insurance one must die to win," which merely means that the conditions of the policy are such that no direct benefit can be derived during the life-time of the person whose life is insured. They fill an economic function, however, in that they provide adequate protection against death without a sufficient estate to provide for those dependent.

The *endowment policy* contains the provision that the insurance company will, at the end of a stated term, usually ten or twenty years, pay a stated sum to the person insured, regardless of death, or that if death occurs before that time the sum will be paid at the time of death. It is popularly designated as "invest-

ment" insurance, because it provides, not only for protection against death, but also for a return of the fund invested in the form of premiums.

The premiums for this kind of insurance are much higher than for straight life insurance, because the company not only insures the life of the insured but promises a return at the end of a stated period if the insured does not die.

**394. Parties.** There are three parties to contracts of life insurance. These are: (1) The insurer, being the person or company assuming the risk; (2) the insured, being the person taking out the policy and with whom the contract of insurance is made; and (3) the beneficiary, being the person to whom the money is to be paid upon the death of the insured.

The second person is generally person whose life is insured, though not necessarily so.

The third person, the beneficiary, is sometimes eliminated as a separate person, by the insured taking a policy payable to himself or to his "estate," and in the event of his death the money is treated as any other part of his personal property, and distributed among his heirs accordingly.

**395. Insurable Interest.** The person paying the premiums must have an insurable interest in the life insured in order to create a valid contract of insurance. One, of course, has such an interest in his own life, and a creditor also has an insurable interest in the life of his debtor to the extent of the debt. A partner has an insurable interest in the life of his co-partner, and a child, if dependent on a parent for support and education, has such an interest, as also has a parent if dependent upon his child for support. A married person has an insurable interest in the life of his wife or her husband.

In life insurance it is sufficient if this interest exists at the beginning of the policy. (In fire insurance an insurable interest must continue throughout the life of the policy.)

Blood relationship is strong proof of an insurable interest, though it is not conclusive, and the rule is generally observed, except in New Jersey, where the doctrine of insurable interest is immaterial in life insurance policies, that there must be some

pecuniary interest, not wholly contingent and remote, in the person whose life is insured.

If an applicant for life insurance has paid premiums but no insurance has been effected, as would be the case if the company should show that he had no insurable interest, he may as a rule recover the premiums paid, unless he has been guilty of fraudulent misrepresentation. This is because the consideration has failed. If, however, the risk has in fact attached, although it has afterwards terminated, and the insured has therefore had some benefit from the contract, he cannot recover the premiums. This might happen if the insured has violated some term of the policy so as to give the insurer the right to cancel the policy.

EXAMPLE

A college which had received many gifts from its founder, purchased a policy of insurance on his life, paid the premiums, and on his death claimed the amount of the policy. Its right to receive this was denied by the courts, as the college had no insurable interest in the life of its founder, there being a mere speculative expectation of future advantage. Trinity College vs. Insurance Company, 113 N. C. 244.

**As to Beneficiaries.** The general rule is that the beneficiary of a life insurance policy does not need to possess an insurable interest in the life of the insured. This is because the beneficiary is not a direct party to the contract. The contract exists for his benefit, but it was created between the insurer and the insured, and an insurable interest in the life insured, possessed by the person contracting, is sufficient.

**396. Assignment of Policies.** Policies usually contain provisions in reference to their assignment, and when they do, the provisions are binding. It is no uncommon thing for policies to be assigned for security or otherwise, and the usual requirements are that notice to the company and its assent to the assignment are necessary to validate it, and in addition there must always be a delivery of the policy to the assignee. An invalid or unauthorized assignment of a policy does not destroy its validity, but is a mere nullidity, and leaves the insurance money payable to the parties originally designated in the policy.

**397. Representations and Warranties.** The same general principles as to representations and warranties apply in life insurance as apply in fire insurance. It is sufficient if the answers to questions in the application blank are stated with substantial accuracy, unless there is actual fraud, and words and phrases are given their ordinary meaning.

EXAMPLE

The question, "To what extent do you use alcohol?" was answered, "None." The policy could not be avoided by the company for misrepresentation by showing an occasional use. Grand Lodge vs. Belcham, 145 Ill. 308.

Nor will the falsity of volunteered information avoid the policy unless it was both material and relied upon by the company.

EXAMPLE

The question, "To whom do you wish your insurance payable in the event of death?" was answered, "To my wife, Emily Louise Vivar." This woman had not yet become the applicant's wife, but this did not avoid the policy, for the information was not material, and the beneficiary was sufficiently designated. Vivar vs. Supreme Lodge, 52 N. J. L. 455.

It is customary to incorporate answers to questions regarding the physical condition and health of the applicant in the policy of insurance. Statements so made are warranties and must be substantially true or the company may refuse to perform its contract. The good faith of the applicant will be insufficient, if the statement was actually false.

EXAMPLES

1. Grattan applied for a policy of life insurance, naming his brother as beneficiary. He answered an inquiry on the policy as to the condition of his health, by stating that he had "good health." Upon his death his brother sought to recover the insurance money and the company sought to avoid the policy by showing that Grattan had dangerous symptoms at the time of issuance of the policy and was not in good health. The brother was permitted to recover, for the term "good health" refers to the general condition in which one believes oneself. Grattan vs. Insurance Company, 92 N. Y. 274.

2. Yung stated in answer to a question in a policy that he did not have Bright's disease. As a matter of fact he was in an advanced stage of the disease, though he did not know it. The company could avoid the policy. Insurance Company vs. Yung, 113 Ind. 159.

**Incontestable clause.** Most insurance policies provide that after a stated period, usually one or two years from the issuance of the policy, the company cannot avoid the policy on the ground of misrepresentation or breach of warranty by the applicant at the time of the issuance of the policy. This is to protect the policyholder, and is based upon the idea that the company should discover any facts which it intends to take advantage of within that time and should not be permitted to allow the insured to continue paying premiums if the policy is to be avoided. By this clause the company waives all defenses, except that of insurable interest, which is a requirement imposed by public policy and cannot be waived.

**398. Payment of Premiums.** It is usual for insurance policies to contain a clause requiring premiums to be paid on or before a certain fixed date. If the company should accept an overdue payment of premium, the right to object to the delinquency is waived.

The amount of the premium in life insurance is based upon tables of average life of persons of the age of the applicant, called mortality tables. The premium is increased with the age of the applicant.

**399. Deaths Covered by Policy.** Not all deaths are covered by a life insurance company, among the usual limitations being that the company shall be relieved from paying insurance if the insured is executed as a criminal by the state, or is killed while engaged in the commission of a crime. Much confusion has resulted over the question as to the liability of an insurance company to pay for death by suicide. The American courts have generally allowed recovery for death by suicide on the ground that the person committing the act of self-destruction is insane at the time, and is not committing the act for the purpose of defrauding the company which has insured his life. If it be shown, however, that the taking out of the insurance was a part of a fraudulent scheme, payment may be successfully contested. It is now customary for policies to provide that they are incontestible in the event of suicide committed at any time after three years from the time of their issuance.

## CASUALTY INSURANCE

**400. Casualty Insurance** includes a great variety of policies, covering many different forms of risks. The condition upon which the insurance company agrees to pay for a loss is that some accident shall injure the person or property of the insured. The form of policy may be either open or valued, the latter being often adopted in the case of personal accident insurance an agreed valuation being fixed for certain injuries, as the loss of a limb, the loss of an eye, or death. New forms of casualty insurance are being constantly created to satisfy the demands of the commercial world, which through this medium seeks protection against the uncertainties of trade and commerce.

**Personal Accident Insurance.** This is insurance by which the insured is protected against accidents causing him personal injury. The amount of premium is regulated by the hazard incident upon the business in which the insured is engaged. The indemnity is conditioned for payment upon circumstances resulting from an external, violent, and accidental cause. Thus a death by accidentally inhaling gas, or by drowning, is the result of an external cause, as is illness caused from poisons. Violent causes may include even slight physical injuries, such as the sting of a bee, the contact of an injurious substance with the skin, resulting in blood poison, and even an injury resulting from fright. Accident policies usually provide a complete list of payments which will be made by the company upon the happening of specified events, and as the forms of policies differ materially, no valuable generalizations can be made.

**Employers' Liability Insurance** is designed to protect employers against liability for injuries sustained by workmen in their employ. The agreement on the part of the company is to indemnify the insured, in the event that he becomes legally liable to pay damages, and to undertake to make all legal defense necessary.

**Title Guaranty Insurance** is a means popular in the larger cities, of protecting the purchasers of land against defect in the title previous to their ownership. The insurance company, through its attorneys, investigates the title and then guarantees, or insures it, against defects.

**Plate Glass Insurance** protects the owner of glass windows against loss by breakage, the insurer of the glass usually replacing it upon breakage.

**Steam Boiler Insurance** is designed to protect the owner or occupant of a building against immediate loss or damage caused by the explosion, collapse, or rupture of a boiler, and protects the insured against personal responsibility to others by reason of such breakage.

**Fidelity Insurance** protects employers against the dishonesty of their employees, or against the wrongful acts of others occupying positions of trust.

**Credit Insurance** protects the business man against loss caused by the dishonesty or insolvency of his debtors.

**Burglary Insurance** protects against loss by theft.

In addition to these many forms of casualty insurance, new forms are constantly being devised, such as Automobile Insurance, Rent Income Insurance, Insurance against Sickness. The premiums vary with the nature of the risk. Hail and Cyclone insurance is popular among farmers, protecting them against damage to crops by these causes.

Many of these forms of insurance are issued by mutual companies in which the fund for the payment of losses is collected by annual assessments upon the members, but in nearly every form it is also possible to find an insurance corporation which will assume the risk upon the advance payment of an annual premium.

## REVIEW QUESTIONS

1. Ames, a creditor of Bates, took out an insurance policy on Bates' life for $15,000. Bates at that time was indebted to Ames for $1200. What objection, if any, might be made to this policy and by whom?

2. Sarah Innes, an orphan, was reared by George Carpenter. She was never legally adopted by him, however, although he paid her various expenses, including a course in a university. When she was twenty-two, she insured Carpenter's life for $20,000, payable to her on his death. What objection, if any, might be made to this policy and by whom? Why?

3. Paterson insured the life of a woman to whom he was married, and whom he supposed to be his wife. As a matter of fact she had another husband living from whom she had not been divorced, so that the marriage to Paterson was a nullity. Upon her death may Paterson recover the amount of the policy? Why?

4. Wilkinson in answer to the following question in an application for life insurance, "Have you ever met with any accidental or serious injury, and if so, what?" answered "No." The company, when sued for the insurance money after his death, defended on the ground that he had, several years before taking out the policy, fallen a considerable height from a tree and was sick for two weeks at the time, but that this in no way contributed to his death. May the beneficiary recover? Why?

# CHAPTER XLV

## REAL ESTATE

### ESTATES

- I. As to Length
  - 1. Inheritable, or estates in fee-simple
  - 2. Non-inheritable
    - a. For life
      - Dower
      - Curtesy
      - Homestead
    - b. For a term of years
- II. As to Time of Enjoyment
  - 1. In possession
  - 2. In Futuro, or in the future
- III. As to Number of Owners
  - 1. In severalty
  - 2. By joint tenancy
  - 3. By tenancy in common

**401. Real Property** consists of the right in lands and such things as are permanent, fixed and immovable. It includes rights in the minerals that are beneath the surface of the earth, water flowing upon it, and things of a permanent nature attached to the earth, such as buildings, trees, and the unsevered fruits of the soil.

**402. Source of Real Estate Law.** The laws respecting real estate were developed at a very early period in England, and the English conceptions became fully implanted in the colonial minds before the separation of the United States from Great Britain. These conceptions have continued to the present time, and the early English law is even now frequently quoted as authority for decisions respecting real estate, and in interpreting rules.

The English law regarding real estate was developed while England was under the feudal system of government, the feudal system having itself been a development from the Roman law and the primitive customs of the early Teutonic tribes. It was

introduced into England from France by William the Conqueror, and formed the basic theory of real estate law. By that theory the original title to all land vested in the king, who was deemed to hold it and to rule by divine right. Immediately below him were the great nobles, the king's tenants in chief, among whom the lands were parceled out in large districts to be held by them in return for military service to the king. The estates of the nobles were in turn re-parceled among under lords, and again and again until the earth-tenant, or the actual cultivator of the soil, was reached. Each holder was bound to return money or services to his superior, the title to the lands being always ultimately traceable to the king, or over-lord.

Under the feudal system several forms of tenure, or land holding, developed, varying in the character of the duties owed to the superior lord, and the rights possessed by the tenant. These underwent various changes until in the year 1645 practically all the tenures came to be known as "freeholds," by which name all estates in land have been known since that time, with the exception of a few English church estates.

In the United States, the title to all lands is considered to have been originally derived, since the Revolution, from either the state or the United States. The idea of feudal dues and obligations has, however, been eliminated from our law, and the ownership of land is absolute and unconditional in the owner, except as against the right of the state to purchase land for public purposes by the power of eminent domain, even against the will of the owner, the right of escheat, and the right of the government to enact regulations by virtue of its police power.

**403. An Estate** is the nature and extent of the interest which a person has in real property. There are many different kinds of estates in land, the most important being as shown in the outline at the beginning of this chapter.

**404. Fee Simple.** This is the largest estate possible to be possessed in property. It is the absolute ownership and title, and may be defeated only by the state under its power of eminent domain, escheat, or police power. The owner holds it not only for his own life, but he owns that future enjoyment which will descend to his heirs according to the laws of descent. This is the

common manner of holding land in the United States. The owner in fee simple may use the property as he may see fit, or he may dispose of it to whomever he chooses by deed or will.

**405. Life Estate.** Instead of being possessed of the absolute title to land, a person may hold it only for the term of his own life, or the life of some other person. Such an estate is known as a life estate. It is not an estate of inheritance, for he who owns it, known as the life-tenant, possesses no rights extending beyond his own life, or the life of the other person whose life is designated to measure the term of the estate.

The life tenant has the right, however, to the full use of the land, and all its profits, during his estate. He may cut all necessary wood for his fuel and to repair his fences and buildings, during the continuance of his estate, but he is not entitled to commit acts which materially injure the future value of the estate, these acts being known as *waste*, and being wrongful on his part. This may be either *actual* or *permissive* waste, permissive waste occurring when buildings are allowed to decay. In the absence of agreement, the tenant is bound to keep the premises in as good repair and condition as he found them, inevitable accidents excepted. The tenant for life is likewise bound to pay the taxes and interest on incumbrances.

The life tenant is also entitled to *emblements*, these being the annual crops growing on the land at the termination of the estate. The theory for allowing the life tenant these crops is that he could not forsee the time of death of the person on whose life the estate depended, and should be entitled to crops which he had planted in expectation of reaping. The life tenant may part with his estate or any portion of it, but cannot lease or grant it to another for a period to extend beyond the life estate.

A life estate may be created by deed or by will, or by operation of law. The rights of dower, curtesy, and homestead are created by operation of law.

EXAMPLE

Brown, dying, left a will giving all his real property to his wife to be held and enjoyed by her as long as she should live. On her death their children were to come into possession and enjoyment of the property. The wife had a life estate.

**406. Dower** is the right which a wife has, upon the death of her husband, in lands which her husband owned in fee simple, while she was under his protection. It is a life estate in one equal third part of all such lands, and is a right of which she cannot be deprived by any act of her husband. She may, however, waive it by joining with him in a deed during his lifetime, or she may herself convey it either before or after his death. She may also abandon her right to dower by accepting a provision in her husband's will giving her other property instead of the dower interest. The right of dower is for the protection of the wife and she is not compelled to accept a provision in a will giving her other property, unless she so desires. She cannot ordinarily have both the dower right and the property left her under a will, but must disclaim one or the other. In some states this right has been limited by statute, and in others enlarged, though in general the common law right of dower, as previously defined, remains unchanged.

EXAMPLES

1. Ames dies possessed of 640 acres of land, leaving a widow and several children. He leaves no will. The widow is entitled to receive the rents and profits of one-third of this land for her life. The remaining two-thirds would be immediately distributed among his children and the one-third in which she had her dower right would go to the children at her death.

2. Bates, in contemplation of marriage, made an agreement with his prospective wife by which she accepted stocks and bonds to the value of $10,000 instead of dower. At Bates' death, she would not be entitled to any dower in property owned by her husband.

3. Call, a married man, sold some of his property, known as Blackacre, to Dale, Call's wife not joining in signing the deed from Call to Dale. After Call's death, Mrs. Call may assert her dower right in this property.

**407. Estate by Curtesy.** At common law the husband acquired by his marriage the right to all of the rents and profits from his wife's property, and at her death, if a child had been born to them capable of inheriting from her, the husband became entitled to an *estate by curtesy*, which was a life estate in *all* the real property which his wife had owned in fee during their marriage relationship. Many states have abolished this right of the husband*; others have limited it to a right equivalent to

* California, Colorado, North Dakota, South Dakota, Georgia, Idaho, Maryland, Iowa, Kansas, Maine, Minnesota, Nevada, Washington, Mississippi, South Carolina, and Wyoming.

a dower right†; and still others have modified the right so as to give it effect even though no child be born.‡

**408. Homestead.** This is a life estate which is of purely statutory origin and did not exist at common law, but now prevails throughout the United States. It is the right to a life interest in a certain amount of land, which right is given to the head of a family and cannot be seized to satisfy the demands of creditors. The extent and value of land allowed as a homestead differs widely in the various states, and the statutes of the particular state must be consulted to determine its limits. The policy of law permitting such an exemption from the claims of creditors is one of protection for the community against the possibility that persons will be made public burdens if creditors take all of their property, leaving them not even a home.

The claim to a right of homestead attaches to practically all estates known to the law, but a common requirement is that the person claiming this right must reside upon the land and actually make it his home, and that he must have a family dependent upon him.

In some states the widow has a right to exercise this right of homestead after the death of her husband, so that she not only has her dower right to one-third of his real estate in general for her life, but also the entire life estate in a limited part which is her homestead. The signatures of both husband and wife are required to convey a homestead interest to a purchaser.

**409. Estate for Years.** This is the estate generally designated as a lease. The common designation is a figure of speech, substituting the name of the instrument by which it may be conveyed for the estate itself. An estate for years, no matter for how long a term, is considered personal property, and has none of the dignity attached to a freehold, which is an estate of inheritance, or a life estate. An estate for years may be created to continue for a much longer period than a life-estate, but it is nevertheless regarded by law as inferior to a life-estate. Estates for years are created by a contract or lease, and may be created by

† Illinois, Kansas, and Maine.

‡ Michigan, Ohio, Nebraska, West Virginia, and Oregon.

parol contract as well as by deed, unless the agreement falls within the provisions of the Statute of Frauds, which generally limits leases which may be created by parol contract to leases for a period less than one year.

**410. Future Estates** may be either estates in *reversion*, or in *remainder*. These are terms adopted by the common law to designate particular estates in land to which the owner does not have the right to immediate possession, but which he owns and to which he will acquire the right to possession at a future period.

If one grants a life estate to another, the property to come back to the grantor at the end of the life estate the grantor is said to have an estate in *reversion*, for it reverts to him.

If one grants a life estate to another, the property to go to a third party at the end of the life estate, the third party is said to have an estate in remainder, for he gets what remains at the end of the preceding estate.

EXAMPLES

1. Ames, who owns a tract of land, known as Whiteacre, by deed grants an estate in Whiteacre to Bates for his life. Ames retains as an estate in reversion all the interest in the land after the death of Bates. Should Ames die before Bates, Ames' heirs will be entitled to receive the land upon the death of Bates.

2. Call, owner of Greenacre, by deed grants a life estate to Dale, and upon the death of Dale a second life estate to Eagan, the remainder upon Eagan's death to go to Fuller. Fuller's estate is a remainder in fee simple, while Dale and Eagan take life estates in the same land, Eagan's right to possession being postponed until Dale's death.

Estates in remainder may be either *vested* or *contingent*. If the person to whom is granted an estate in remainder is alive at its creation it is a *vested* interest, only the enjoyment and possession being postponed. If the person who will enjoy the remainder is unborn, the estate is *contingent*.

It is important to know that contingent remainders cannot be created to take effect at an unreasonably distant time, for otherwise restrictions might be placed upon property which would interfere with its use by all future generations. The Rule Against Perpetuities prevents this. It usually is stated as follows: No future interest in property is valid unless it must

by its terms become a vested remainder within twenty-one years after the death of some designated person* living at the time of its creation. The application of this rule is extremely technical and no attempt should ever be made to restrict the use of property by creating contingent remainders without consulting a skilful lawyer.

**411. Eminent Domain.** A sovereign state has the right and power to take private property for public uses for the purpose of promoting public welfare. This is usually done by a legal process known as condemnation proceedings, in the course of which the fair market value of the land is determined by the court. This amount is then paid by the state to the owner of the land taken, and the owner cannot object to the sale of the land. Land for railroad rights of way, telephone purposes, and telegraph purposes is frequently secured in this manner, the state granting these companies the right to exercise this power of eminent domain because of the public nature of their business.

**412. Escheat.** If no owner or lawful claimant of the land can be found, the title to the land so left without a proprietor reverts (escheats) to the state. The procedure necessary to revest the title in the state is prescribed by statute.

**413. Police Power** is the power of the state to make reasonable rules and regulations, even though they restrict the right of an owner of land as to its use, for the purpose of promoting public welfare and good government.

**414. Easements** are rights which the owner of land may grant to another to use the land in a certain manner, but not to own it. For example, it is customary among farmers for one farmer to have a right of way across the land of a neighbor, or for the owners of adjoining buildings to erect a common stairway and grant to each other the right to use the entire stairway indiscriminately. Use of another's land by way of easement for a long period of time, usually provided by statute to be twenty years, raises a presumption that the easement was once granted and the deed lost, and it will then become a perpetual right.

* In some states, the additional twenty-one year period is omitted.

EXAMPLE

Williams and Barlow own adjoining store buildings in Chicago, a common stairway in William's building being the only means of access to the upper floors of both buildings. If Williams grants Barlow the right to use this stairway, Barlow has an easement.

**415. How Property is Held.** The nature of ownership in severalty, in common, and in joint tenancy was discussed in its relation to personal property in an earlier chapter. (See Sec. 17.) In addition to what is there said it may be added that the title to real estate is frequently held by a third person, called a *trustee*, who has no right to use the land. In such cases the trustee merely holds the naked title for the benefit of the true owner, called the beneficiary of the trust, to whom he must account for all the profits and proceeds of the land.

EXAMPLE

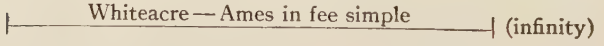
Ames, by his will, devises Blackacre to his brother, John, to hold as trustee for a minor son of Ames. The minor son is entitled to all the profits of the land, John merely holding the legal title for his benefit. This manner of holding land is adopted to prevent its waste by improvident or irresponsible persons, at the same time allowing them to enjoy the benefits of ownership.

## GRAPHIC REPRESENTATION OF ESTATES IN LAND

The nature of these various forms of estates in land is one of the most difficult legal points for the layman to grasp. They rest entirely upon the medieval conceptions of the nature of real property, and can be best explained by adopting the medieval idea of treating the title to property as a tangible thing, beginning at the present moment of time and continuing until the end of all time, or infinity.

Let the following straight line represent the title of Ames in a parcel of land, Whiteacre, which he owns in

### Fee Simple

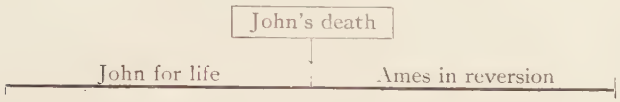



This is the greatest and highest estate known to the law and indicates that Ames controls both the present and future use of

the land and that it belongs absolutely to him and to his heirs, or the persons to whom he grants it, forever.

He may dispose of it so as to give his son, John, a

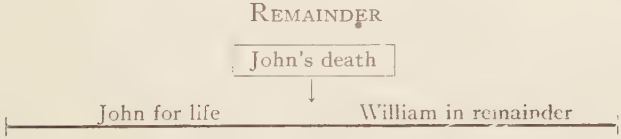
LIFE ESTATE




thereby carving out of his entire estate a lesser estate which terminates upon the happening of a definitely stated event, the death of John. The part remaining after John's death is a reversion, for not being disposed of by Ames it remains with him, and he may either further dispose of it or keep it until his death when it will pass to his heirs. It is an estate *in futuro*, and upon John's death will become an estate in possession.

Or Ames may instead dispose of his land in such a manner as to create a

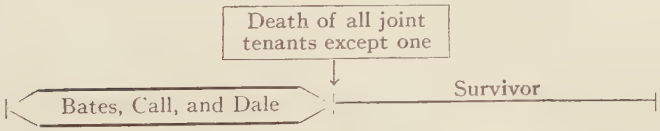
REMAINDER




He does this by granting his son, John, a life estate, the remainder to go to William and his heirs forever. Ames thereby disposes of his entire title, but William does not receive possession until John's death.

Or Ames may dispose of Whiteacre in such a way as to create a

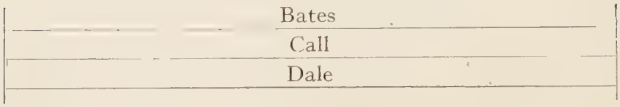
JOINT TENANCY




Bates, Call and Dale will own the entire property as joint tenants, all owning the same thing at one and the same time, and on the death of either his share going to the others, until finally the last survivor will own the entire estate in fee simple.

Or Ames may create a

TENANCY IN COMMON




Bates, Call and Dale, will in that event each own an undivided one-third interest in Whiteacre, but, unlike an estate in joint tenancy, upon the death of any one his share will go, not to the survivors, but to his own heirs, for the estate of each is a fee simple in an individed one-third of the land.

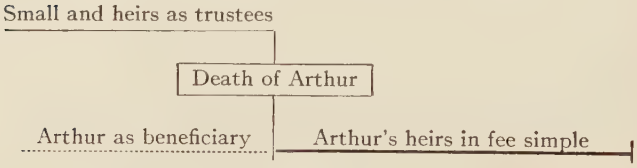
Or Ames may rent a portion of the land to Tupper for a

TERM OF YEARS

This is not an estate of inheritance, but merely a right of use for a term of years, and the title continues vested in Ames, subject to the outstanding right of Tupper to use the land.

Or Ames may create a

TRUST ESTATE




He may do this by leaving Whiteacre by his will to Small and his heirs, as trustees, to hold the land for the use and benefit of Arthur Ames, and on the death of Arthur Ames, the title to vest forever in his heirs. Small and his heirs hold only a naked legal title. They hold this title only during the life of Arthur Ames. They have no right to the beneficial use or enjoyment of the land.

## CHAPTER XLVI

## REAL ESTATE CONVEYANCES

**416. How Title is Transferred.** With the nature of the various estates in land common in the United States in mind, the different instruments of conveyance, by means of which these estates may be transferred from one owner to another, will be considered. As the estates themselves have their origin in the feudal system, so the instruments of conveyance were also taken from the same military age, and this fact accounts for much of the general form and phraseology of these instruments.

Title to land may be transferred from one owner to another by either (1) descent, or (2) purchase. Title by descent is acquired when the owner dies and the estate of which he was the owner passes to his heirs. Title by purchase is acquired by means of one of the several instruments of conveyance in the life-time of the owner.

**417. Conveyances** of land from one owner to another are made by formal instruments, the forms of which are generally provided by statute. The instrument by which the *absolute title* of a freehold, or estate of inheritance, is transferred from one owner to another, is called a *deed*. The conveyance for a term of years is called a *lease*, the owner being designated as the *landlord* and the person receiving the leasehold interest the *tenant*. Conveyances for purposes of securing debts, or *conditional conveyances*, are called *mortgages* or *trust deeds*, depending upon their form, and are more fully discussed in the following chapter.

**418. Deeds,** as used in commercial transactions, are of two kinds: (1) Quitclaim deeds, and (2) warranty deeds. By means of a quitclaim deed, the owner of land, called the *grantor*, relinquishes all the estate which he possesses in a particular tract of land, substituting the person receiving the deed, called the *grantee*, as the owner of whatever rights he may have had. The effect of a quitclaim deed is to transfer the title which the grantor

had, throwing upon the grantee all risk as to whether the grantor's title was perfect or defective.

By the warranty deed, the grantor not only conveys the designated estate to the grantee, but further covenants and warrants that he actually owns all the estate which he purports to convey and will defend it against the claims of other persons. The warranty deed is a much safer deed from the standpoint of the grantee, for by it not only the grantor, but usually his heirs, are bound to protect the ownership of the grantee and his heirs forever.

All deeds are writings sealed and delivered between the parties. The material upon which they are written is parchment or paper. They must be made by a party able to contract, and must be founded upon some consideration. Their terms must be set forth legally and in an orderly fashion. They must be free from any erasures and interlineations which are not explained in writing on the face of the deed itself. In some states, signing by the grantor, and the attestation of his signature by one or more witnesses, and his acknowledgment of the instrument as his deed before a notary public or magistrate, are necessary. The public recording of a deed is not essential to its validity, but is designed to protect the grantee against the claims of the grantor's creditors, and of subsequent *bone fide* purchasers.

The grantee of a deed should assure himself:

1. That it be in writing.
2. That the grantor is a competent party.
3. That the estate to be conveyed be definitely described.
4. That a consideration be expressed.
5. That it be duly executed.
6. That it be delivered.
7. That it be registered in a public office to affect the rights of third persons.

The sufficiency of the writing, the competency of the parties, and the adequacy of the consideration, are governed by the principles which were fully discussed under the subject of contracts. The property, or estate, to be conveyed must be clearly

described in the deed, both as to its nature and extent, as well as its location. The congressional system of survey provides an excellent method for legal descriptions, which may be supplemented by reference to town plats, or sub-divisions, street numbers, water-courses, monuments, or other points definitely fixed by nature or by law, depending upon the location of the land.

EXAMPLES

The following are typical legal descriptions in deeds:

*The Southeast quarter* ($SE\frac{1}{4}$) *of the Northwest quarter* ($NW\frac{1}{4}$) *of Section twenty-nine* (29), *Township thirty-eight North* (38 *N*) *of range fourteen* (*R*14) *West of the third principal meridian.*

*Beginning at the Northeast corner of Lot Twenty-two* (22) *of Fuller's Addition to the city of Lancaster, as more fully appears by the recorded plat thereof, thence west one hundred twenty-two* (122) *feet, more or less, to a certain stone monument, thence south seventy-one* (71) *feet, thence east one hundred twenty-two* (122) *feet, more or less, to the front line of said lot, thence north along the front line of said lot seventy-one* (71) *feet, to the place of beginning; all said land being in Grant County, Wisconsin, Section Twenty* (20), *Township Twenty* (20) *North of Range Five West of the fifth principal meridian.*

The last description is said to be "by metes and bounds."

*Execution.* The due execution of a deed includes the four essentials of signing, sealing, attestation, and acknowledgment. A deed is required to be signed by the grantor, either in person or by an agent authorized under a sufficient power of attorney. If such an agent sign the deed, it must appear both in the body of the instrument and by the signature that he signed it for, and in behalf of, the grantor, and that he was empowered to do so; thus, James E. Smith, by E. A. Brown, Atty. If the grantor is an illiterate person, incapable of signing his own name, he may execute the deed by making a cross, or other device, called his *mark*, in the presence of witnesses.

*Sealing.* The formality formerly attendant upon the sealing of an instrument has been made by statute somewhat less burdensome, though the majority of the states still require a seal in some form on instruments of conveyance of land. The seal need not be of any particular form or material, so long as it has been adopted by the grantor as his seal. The deed should contain a recital that the grantor has affixed his seal as a further evidence of his intention to execute a sealed instrument.

**In Witness Whereof** *the parties of the first part have hereunto set their hands and seals the day and year first above written.*

*Signed, Sealed, and Delivered*
*in the Presence of*
*J. L. TALBOTT.*
*J. H. SMITH.*

*CHARLES HATHAWAY.* [Seal]
*LAURA HATHAWAY.* [Seal]

*Attestation.* Witnesses of the signing, sealing, and delivery are sometimes required to sign a deed in order to give it a full legal effect as an instrument of conveyance. Their function is to prove the signatures of the parties, and no particular formality is attendant upon their signature. It is only necessary that the grantor, for whom they are witnesses, shall have acknowledged in their presence that the signature on the instrument is his.

*Acknowledgment.* Every deed, as a part of its due execution, should be acknowledged. The grantor or grantors should appear before some officer authorized by law to take acknowledgments, and state that they have signed and sealed the instrument with full and complete knowledge and understanding of its contents. If dower or homestead rights are to be released, the officer should inquire particularly if such rights are waived, and some states require that the wife be examined separately and apart from her husband so that no force or coercion may be used in procuring her acknowledgment to the deed.

Notaries public, court officials, and justices of the peace, are the officers usually empowered to acknowledge deeds, and such officer should attach his certificate under his official seal to the deed. The objects of acknowledgment are: (1) To admit the deed to record; (2) to provide an additional safeguard against fraudulent conveyances; and (3) to furnish a further means of identification of the grantor and additional proof of the due execution of the instrument by him.

EXAMPLE

*State of Wisconsin* } ss.
*County of Calumet* }

**Be It Remembered,** *That on this 22d day of June, A. D.* 1916, *personally came before me the above named John Harris, and Samantha, his wife, to me known to be the persons who executed the foregoing deed, and acknowledged the same to be their own free act and deed for the use and purposes therein mentioned.*

*WALTER WHEELER,*
*Notary Public, Calumet County, Wisconsin.*

(Official Seal)

When the property conveyed consists of the homestead and the wife signs the deed, the statutes of some states* require that the acknowledging officer shall certify that he has satisfied himself that the wife was aware that she was parting with her homestead rights. In Illinois it is also required that the certificate shall also show a distinct release of the right of homestead. The same doctrine is applied in some states to the release of dower.

*Delivery.* It is essential to the validity of a deed that it be delivered to the grantee, this delivery implying that the grantee has by his acceptance of it become bound by the bargain. The delivery must be made with the intention to transfer the title to the grantee, for if a deed is stolen or obtained by fraud, before a valid delivery, it has no effect and there is no transfer of title. A deed is presumed to have been delivered on the date of its execution, but the true date of delivery may be shown for the purpose of establishing the time at which the deed became effective. When the grantor wishes to make a conditional delivery, the deed may be left with a third party, to be delivered to the grantee upon the performance of the stipulated conditions. This is called a delivery *in escrow*, and the third party, except at his own peril, cannot deliver the instrument until the conditions have been complied with.

*Recording.* The system of recording titles is common to all states. It is an admirable feature of our real estate law, as it gives to all persons who have occasion to deal in land reliable means for ascertaining all material facts with regard to the title. Deeds are recorded with a public officer, generally the county recorder, or register of deeds, in the county in which the land is situated. The public officer notes on the instrument the day and hour of the filing, and the instrument is then copied into the county records. This serves as notice to the public at large of the conveyance, for the records are open to the public. The original deed is returned to the owner, and if it be mislaid or lost, the public record serves in its stead.

If two deeds are in existence at the same time, the grantee of the deed first recorded has *prima facie* evidence that he is the

* Alabama, Florida, Kentucky, Texas, and Wyoming.

owner of the property. His priority of registration is of no use to him, however, if it be proved that he knew of the existence of another valid deed. Subsequent purchasers who buy in good faith without knowledge of the unrecorded instrument are protected under the law requiring recording.

*Torrens Registration.* In order to simplify land titles, and eliminate a part of the expense incident upon an examination of the public records of title to lands, some of the states have adopted a system devised in New Zealand, known as the Torrens System of Land Registration. It provides a means by which the owner of land may petition a court of proper jurisdiction to have his land registered under this system, and after a careful examination of the title, the court issues a decree, or order, stating the title or interest of the applicant, which may then be registered. A certificate is issued, which shows the name of the owner, whether the owner is married or unmarried (unless a corporation is owner), and if married, the name of the husband or wife; if the owner is a minor it states his age, and if he is under any other disability, the nature of the disability. The nature of the estate, whether legal or equitable, the description of the premises, and all existing liens, mortgages, incumbrances, and charges to which the owner's title is subject, are also noted. Subsequent transfers of title can be readily made by a transfer of the certificate showing title, and new certificates are then issued to the new owners without the necessity of a further search of the records for prior liens.

The component parts of a deed are:

1. Premises.
2. Habendum (to have).
3. Tenendum (to hold).
4. Reddendum (reservations).
5. Conditions.
6. Covenants.
7. Warranties.

The only essential one of these is the first, the premises. If that be included, a deed, however informal, will be effective in passing the title, provided of course that it contains some expression of an intent to convey the land described, and is duly executed and delivered as the deed of the grantor to the grantee.

*Premises.* This should contain the names of the parties, the consideration, words of explanation, identification of parties by residence, the description of the property granted, with the exceptions or reservations, if any, the words of grant, and usually the estate or quantity of ownership.

**419. Warranty Deeds.** A warranty deed is shown herewith, in sections, each section being separately shown and discussed.

### Warranty Deed

#### Premises

**This Indenture,** *Made this 22d day of June, in the year of our Lord one thousand nine hundred and fourteen,* **between** *John Harris and Samantha, his wife, of Chilton, Wisconsin, parties of the first part, and George Underwood of Chicago, Illinois, party of the second part.*

**Witnesseth,** *That the said parties of the first part, for and in consideration of the sum of One Thousand Dollars, to them in hand paid, by the said party of the second part, the receipt whereof is hereby confessed and acknowledged, have given, granted, bargained, sold, remised, released, aliened, conveyed, and confirmed, and by these presents do give, grant, bargain, sell, remise, release, alien, convey, and confirm unto the said party of the second part, his heirs and assigns forever, the following described real estate, situated in the County of Calumet and State of Wisconsin, to-wit:*

*Lot One (1) of Smith's Addition to the City of Chilton, according to the recorded plat thereof,*

**Together** *with all and singular, the heriditaments and appurtenances thereunto belonging, or in anywise appertaining, and all the estate, right, title, interest, claim, or demand whatsoever of the said parties of the first part either in Law or Equity, either in possession or expectancy of, in and to the above bargained premises, and their hereditaments and appurtenances.*

*Habendum* (to have) and *Tenedum* (to hold). These clauses follow the usual words "to have and to hold," and define the quantity of interest or estate which the grantee is to take in the lands. They are not essential to the validity of the deed, and in the event that they do not agree with the terms of the premises, are secondary to the premises in weight. The *habendum* may limit or qualify the operation of the premises, as by changing the character of joint tenants to tenants in common. It is the proper place to insert declarations of trusts, or to name the grantees if their names do not appear in the premises.

The tenendum clause refers to the feudal system of holding lands as a grant from an over-lord, and has never been of importance under our law, though the name and form is still preserved, appearing in the form of the words, "to hold."

**Habendum et Tenendum**

**To Have and To Hold** *the said premises above bargained and described unto the said party of the second part, with the appurtanances thereunto belonging, unto the said party of the second part, his heirs and assigns, forever.*

*Reddendum.* The reddendum clause contains the reservations and exceptions which the grantor wishes to place in the deed. Thus the grantor may reserve to himself the right to receive the rent from the property for his life, or any other benefit issuing from the land itself, or in fact, any part which decreases the quality of the estate conveyed. Or the grantor may desire to except some part of the quantity of the estate conveyed from the description, and this is called an exception, as when the deed describes the property conveyed and adds a clause such as "except the south forty acres of the northwest quarter."

*Condition.* A clause may be inserted in the deed providing that on the happening of some event the estate shall return to the grantor. The condition may be precedent or subsequent, and serves to revest the title to the estate in the grantor upon the happening of the event.

**EXAMPLES**

1. Ames gives a deed to his daughter, Sarah, to have and to hold certain property so long as she shall remain unmarried, the property to go to her husband upon her marriage. This is a condition subsequent, for upon its happening the title passes from the grantee.

2. Bates gives a deed to Call, describing certain property, and providing that Call shall have the title only upon the condition that he shall attain the age of twenty-five years. This is a condition precedent, for until it is performed, Call will receive no estate in the lands.

*Covenants and Warranties.* By these the grantor, not only for himself, but for his heirs, warrants the grantee and his heirs, or assigns, to be secure in the estate granted. If the grantor covenants in behalf of himself and his heirs, they are bound to perform the agreement or pay damages, provided they have

received property from the grantor by descent, but are not liable beyond the amount of the inheritance. There are four customary covenants in a full warranty deed. These may be as follows:

**And** *The said party of the first part, for his heirs, executors, and administrators, does covenant, grant, bargain and agree, to and with the said party of the second part, his heirs and assigns, that at the time of the ensealing and delivery of these presents.* (1) *He is well seized of the premises above conveyed, as of a good, sure, perfect, absolute, and indefeasible estate of inheritance in law, in fee simple, and* (2) *had good right, full power, and lawful authority to grant, bargain, sell, and convey the same in manner and form aforesaid, and* (3), *that the same are free and clear from all former and other grants, bargains, sales, liens, taxes, assessments, and incumbrances, of what kind or nature soever, and* (4), *the above bargained premises, in the quiet and peaceable possession of the said party of the second part, his heirs and assigns, against all and every other person or persons lawfully claiming or to claim the whole or any part thereof, the said party of the first part shall and will* **warrant and forever defend.**

In the event that the grantee or his assigns should be ousted from their possession they may fall back on the grantor or his heirs and demand damages for their loss. In most of the States the measure of damages is the money paid for the property with interest (deducting rents and profits) and the legal cost of defending the suit.

The so-called "special warranty deed" warrants the grantee only against other persons claiming title from the grantor, but does not protect the grantee against prior owners other than the immediate grantor. This form of warranty is accomplished by transposing the words of the warranty clause to read as follows:

**And** *The said A. B. (grantor) for himself, his heirs, executors, and administrators does covenant, grant, bargain, and agree to and with the said party of the second part (grantee) his heirs and assigns, that the above bargained premises, in the quiet and peaceable possession of the said party of the second part, his heirs and assigns, against all and every person or persons lawfully claiming the whole or any part thereof, by, through or under him and none other, he will forever* **warrant and defend.**

This form of warranty affords little protection to the grantee and is frequently made the instrument of fraud, an unsuspecting party assuming that he is receiving a deed with full warranties.

The "short form" of warranty deed is a form prescribed by statutes in the various States, and contains merely the statement that the grantor agrees to forever warrant and defend the grantee

in the property granted, without specifying the four warranties. Where "short form" deeds are prescribed by statute it is usually provided that all the warranties are implied in them.

**420. Quitclaim Deeds.** As previously stated, a quitclaim deed serves to transfer all the right, title, and interest which the grantor has in the lands at the date of its execution and delivery. It differs from a warranty deed in that it contains no covenants warranting the title, so that the grantee receives only such interest as the grantor has, be it much or little, and the protection of the title against rival claimants is upon the grantee, who is without remedy against the grantor should there be a failure of title.

A warranty deed is to be preferred to a quitclaim deed, by a purchaser, not alone on account of its covenants, but also because a warranty deed conveys both the title to the land described, and any title which the grantor may acquire afterwards. For example, if the grantor does not own the land described in a warranty deed at the time the deed is delivered, but acquires the title later by purchase or otherwise, this after-acquired title is immediately transferred to the grantee named in the warranty deed, by force of its terms.

A quitclaim deed transfers only the title which the grantor had at the time of its execution and delivery.

EXAMPLE

Ames sells to Bates the property Blackacre, and gives a warranty deed, but at the time of the sale Ames' title was defective, another party holding an interest in it. Afterwards, Ames secures to himself the outstanding title by purchase. It immediately is transferred to Bates by force of the warranty deed from Ames to Bates. Had it been a quitclaim deed, however, by which Ames originally sold the land to Bates, this newly acquired title would not have been transferred.

### Quitclaim Deed

**This Indenture,** *Made this 22d day of August, in the year of our Lord One Thousand Nine Hundred Sixteen, between Charles H. Hathaway and Laura Hathaway, his wife, of the City of Chicago, in the County of Cook, and the State of Illinois, party of the first part, and Martin F. Deale, of the Township of Pella, in the County of Ford, and State of Illinois, party of the second part.*

**Witnesseth,** *That for and in consideration of the sum of Two Thousand Dollars in hand paid by said party of the second part, the receipt whereof is hereby acknowledged, and the said party of the second part forever released and*

*discharged therefrom, the said party of the first part has remised, released, sold, conveyed, and quitclaimed, and by these Presents does remise, release, sell, convey, and* **Quitclaim** *unto the party of the second part, his heirs and assigns* **forever,** *all the right, title, interest, claim and demand, which said party of the first part has in and to the following described lot, piece, or parcel of land, situated in the County of Cook and State of Illinois, and known and described as follows, to-wit:*

*The South East quarter (S.E. ¼) of the North West quarter (N.W. ¼) of Section twenty-nine (29), Township thirty-eight north (38 N.) of Range fourteen (R. 14), East of the third principal meridian.*

**To Have and to Hold** *the same, together with all and singular the appurtenances and privileges thereunto belonging, or in any wise thereunto appertaining; and all the estate, right, title, interest and claim whatever, of the said party of the first part, either in law or equity, to the only proper use, benefit, and behoof of the said party of the second part, his heirs and assigns forever.*

**And** *the said party of the first part hereby expressly waives and releases any and all right, benefit, privilege, advantage and exemption, under or by virtue of any and all statutes of the State of Illinois providing for the exemption of homesteads from sale on execution or otherwise.*

**In Witness Whereof,** *the said party of the first part have hereunto set their hands and seals the day and year first above written.*

*CHARLES H. HATHAWAY.* [Seal]
*LAURA HATHAWAY.* [Seal]

## CHAPTER XLVII

### REAL ESTATE CONVEYANCES — Continued

**421. A Mortgage** is a conveyance of a property right as security for a debt, or other obligation. It transfers the title, with a conditional clause providing that if the debt be satisfied, the transfer shall be without further effect. This conditional clause is called the *defeasance* clause. The person giving the mortgage is known as the mortgagor, and the one to whom the mortgage is given is called the mortgagee. A mortgage is executed in the same way as a deed. In case of property so held that it would be required that a wife should join in a deed in order to transfer her rights of dower, it is likewise essential that she should be made a party to any mortgage thereon, except that when a mortgage is given as a part of the purchase money in another real estate transaction, the entire property is bound by the mortgage even without her signature.

#### Mortgage

**This Indenture,** *Made this 24th day of August, in the year of our Lord One Thousand Nine Hundred Sixteen, between Martin F. Deale, of the Township of Pella, in the County of Ford, and State of Illinois, party of the first part, and Charles H. Hathaway, of the City of Chicago, in the County of Cook and State of Illinois, party of the second part:*

**Whereas,** *The said Martin F. Deale is justly indebted to the said party of the second part in the sum of One Thousand Dollars, evidenced by one certain promissory note of even date herewith, bearing 6 per cent interest per annum from date, and due one year from date.*

**Now, Therefore, this Indenture Witnesseth,** *That the said party of the first part, for the better securing the payment of the money aforesaid, with interest thereon, according to the tenor and effect of the said promissory note above mentioned, and also in consideration of the further sum of One Dollar to him in hand paid by the said party of the second part, at the delivery of these presents, the receipt whereof is hereby acknowledged, has granted, bargained, sold, remised, released, conveyed, aliened, and confirmed, and by these presents does grant, bargain, sell, remise, release, convey, alien, and confirm unto the said party of the second part, and to his heirs and assigns* **forever** *all the following*

*described lot, piece or parcel of land, together with all the rents, issues, and profits thereof, situate in the City of Chicago, County of Cook, and State of Illinois, and known and described as follows, to-wit:*

*The South East quarter (S.E. ¼) of the North West quarter (N.W. ¼) of Section twenty-nine (29), Township thirty-eight north (38 N.), of Range fourteen (R 14), East of the third principal meridian.*

**To Have and to Hold** *the same, together with all and singular the tenements, hereditaments, privileges and appurtenances thereunto belonging, or in any wise appertaining; and also all the estate, interest, and claim whatsoever, in law as well as in equity, which the said party of the first part has in and to the premises hereby conveyed unto the said party of the second part, his heirs and assigns, and to their only proper use, benefit and behoof forever.*

**Provided, always,** *And these presents are upon this express condition, that if the said party of the first part, his heirs, executors, administrators, or assigns, shall well and truly pay, or cause to be paid, to the said party of the second part, his heirs, executors, administrators, or assigns, the aforesaid sum of money, with interest thereon, at the time and in the manner specified in the above mentioned promissory note, according to the true intent and meaning thereof, then and in that case these presents and everything herein expressed, shall be absolutely null and void.*

**And in Consideration** *of the money loaned as aforesaid to the said party of the first part, and in order to create a first lien and incumbrance on said premises under this mortgage, for the purposes aforesaid, and to carry out the foregoing specific application of the proceeds of any sale that may be made by virtue hereof, the said party of the first part does hereby release and waive all right under, and benefit of, the exemption and homestead laws of the State of Illinois, in and to the lands and premises aforesaid, and the proceeds of sale thereof, and agrees to surrender up possession thereof to the purchaser or purchasers at such sale, or to any receiver that may be appointed by the court, peaceably on demand.*

(Here insert the same covenants as in Warranty Deed.)

**In Witness Whereof,** *The said party of the first part has hereunto set his hand and seal the day and year first above written.*

*MARTIN F. DEALE.* [Seal]

Additions frequently made to the above form of mortgage are clauses providing, (1) that if the mortgagor fails to pay any installment of interest when it becomes due, the mortgagee may declare the whole debt then due and payable; (2), that the mortgagor is required to keep the building insured in favor of the mortgagee to the extent of his interest, and that upon the failure of the mortgagor to insure the building the mortgagee may do so and charge the expense on the mortgage against the mortgagor; and (3) that the mortgagor must pay all taxes and assessments against the property, and that if he does not the mortgagee

will have the same rights as in the case of insurance. These three clauses are popularly known as the "Option," "Insurance," and "Tax" clauses.

**422. Equity of Redemption** is the right of the mortgagor to receive his property again upon the payment or tender of the full amount of the debt, including interest, at the time it becomes due, or thereafter as provided by law. This equity of redemption is a property right which the mortgagor may sell as any other property. It is generally provided that the mortgagor, or his representative, may exercise this right for a considerable period after the debt has become due and payable, or even after the mortgagee has taken legal proceedings to foreclose the mortgage. This period during which the equity of redemption may be exercised varies in the several states, the usual provision being that it is not barred until a year has elapsed after the signing of a judgment of foreclosure.

EXAMPLES

1. A borrows $5000 on a piece of land, which he is to repay in one year, giving a mortgage to B as security for the loan. At the end of the year he is unable to repay the money, and B claims title to the property under the mortgage. Nine months later A tenders B the sum of $5000 with interest in full and all costs incurred by B. B is compelled to receive this money and relinquish all claim in the property to A.

2. A gives B a warranty deed to his house and lot to secure the payment of a debt due in one year. At the end of one year A is unable to pay the debt, and B claims the land. A has the right to go before a court of equity at any time within the statutory period, explain the transaction, prove that the deed was intended only as a mortgage, tender the amount of the debt with interest, and recover title to the property.

**423. Sale of the Mortgage.** The sale of the interest of the mortgagee is accompished by a deed of assignment of the mortgage, which may be in the following form.

ASSIGNMENT OF A MORTGAGE

**Know All Men by These Presents,** *That I, Chas. N. Holmes, of the City of Peoria, in the State of Illinois, the mortgagee named in a certain mortgage deed, given by Edgar P. Farr, of Sioux City, in the State of Iowa, to said Chas. N. Holmes, to secure the payment of Four Hundred Dollars, dated the 8th day of September, A. D.* 1916, *and recorded in the Recorder's Office of Peoria*

*County, in the State of Illinois, in Book N of mortgages, page 326, in consideration of the sum of Four Hundred and Twenty Dollars to me paid by Albert A. Blair, of Chatsworth, in the State of Illinois, the receipt whereof is hereby acknowledged, do hereby sell, assign, transfer, set over, and convey unto said Albert A. Blair and his heirs and assigns, said mortgage deed, the real estate thereby conveyed, and the promissory note, debt and claim thereby secured, and the covenants therein contained.*

**To Have and to Hold** *the same to him, the said Albert A. Blair, and his heirs and assigns, to his and their use and behoof forever; subject, nevertheless, to the conditions therein contained, and to redemption according to law.*

**In Witness Whereof,** *the said party of the first part has hereunto set his hand and seal the day and year first above written.*

*CHARLES N. HOLMES.* [Seal]

A formal assignment similar to the above form is considered preferable, yet the mere indorsement and transfer of the notes secured by the mortgage carries with it all the rights of the mortgagee against the land.

**424. Second Mortgage.** An owner of property may mortgage it as often as he can find a mortgagee willing to accept a mortgage. These mortgages have preference in the order in which they were given. If the entire property is required to satisfy the debt which the first mortgage was given to secure, the subsequent mortgagees will receive nothing. The payment of the first mortgage advances the second to first place as a claim against the property mortgaged. The second mortgagee may also purchase the first mortgage, and merge the two into one obligation, thus protecting his own interest, for the probability is strong that the property will bring much less than its real worth when foreclosed by the first mortgagee, and leave the second mortgagee remediless.

**425. Remedies of Mortgagee.** A mortgage is drawn to secure the payment of a debt, or the performance of some obligation. This obligation is usually represented by a note which the mortgagor has agreed to pay, and which is fully described in the mortgage. Upon the non-payment of this note two distinct remedies are open to the mortgagee who holds the notes and the mortgage. He may sue upon the note, in which event he will secure a personal judgment against the mortgagor, which will become a lien on all property not exempt; or he may foreclose

the mortgage, which is the legal procedure by which the particular property described in the mortgage is subjected to the satisfaction of the debt. Foreclosure is accomplished by a suit in a court of equity, which will decree that the property shall be sold to the highest bidder, to satisfy the debt, and that any surplus shall be paid over to the owners of the equity of redemption. It is usually also decreed that the mortgagee may have a personal judgment against the mortgagor on the notes for any deficiency in the amount realized from the sale.

EXAMPLE

A owns property worth $10,000 which is mortgaged to B for $4000 on a first mortgage. A offers C a second mortgage on the same property for a loan of $1000. This looks safe, but if C is cautious he will not take the second mortgage unless he can also buy the first mortgage or has $4000 on hand with which he can pay off the first mortgage when due, if necessary, and prevent foreclosure. For under the hammer the property might not be bid in for more than the $4000 due on the first mortgage and this would leave C loser.

**426. Purchasers of Equities of Redemption** must be especially cautious to notice the form of the deed by which they receive their conveyance. One form (the usual form) is for the grantor, who holds the equity of redemption, to deed the property, describing it as "subject to a certain mortgage (describing it)." By the other forms the following words are also added: "which the grantee agrees to assume and pay." There is a vast difference in the legal meaning of these two forms. In the former, if the sale of the premises does not produce enough to pay the mortgage debt, no personal liability rests upon the purchaser. In the latter case, a judgment may be secured against the purchaser of the equity of redemption for any deficiency in the payment of the debt secured by the mortgage, for by the acceptance of the deed he has agreed to pay it.

**427. Recording and Discharging Mortgages.** As soon as the mortgage is delivered to the mortgagee he should immediately record it with the proper county officer. This protects him against all claimants who may thereafter acquire any interest in the property. If he should fail to record the mortgage, and others should acquire interests in the property in ignorance of the mortgage, their interests might become superior to his.

When a mortgage is paid it should be discharged of record, so that the mortgagor's title to the premises may again be clear. This may be done by a personal discharge on the margin of the record by the mortgagee in the presence of the county officer who is custodian of the records, or when this is impracticable, it may be done by a release deed, which is acknowledged and recorded in the same manner as other deeds.

### Release Deed

**Know All Men by These Presents,** *That I, Charles H. Hathaway, of the County of Cook and State of Illinois, for and in consideration of One Dollar, and for other good and valuable considerations, the receipt whereof is hereby confessed, do hereby remise, convey, release, and quitclaim unto Martin F. Deale, of the County of Ford and State of Illinois, all the right, title, interest, claim, or demand whatsoever I may have acquired in, through or by a certain mortgage deed bearing date the 24th day of August, A. D.* 1916, *and recorded in the Recorder's office of Cook County, in the State of Illinois, in Book M of Mortgages, page* 187, *to the premises therein described, as follows, to-wit:*

*The South East quarter (S.E. $\frac{1}{4}$) of the North West quarter (N.W. $\frac{1}{4}$) of Section twenty-nine* (29), *Township thirty-eight north* (38 *N.*) *of Range fourteen* (*R.* 14), *East of the third principal meridian.*

*Together with all the appurtenances and privileges thereunto belonging or appertaining,*

**Witness** *my hand and seal this first day of September, A. D.* 1916.

*CHARLES H. HATHAWAY.* [Seal]

The law does not impose upon the mortgagee the duty of preparing this release, but it does impose upon him the duty of executing it when it is presented to him, together with his reasonable expenses for so doing, and in many States he is liable to heavy damages for a wrongful refusal.

**428. Trust Deeds.** In a trust deed the owner of property conveys title to a third person, called the trustee, who takes the naked title for the benefit of the creditor. Then the creditor, also called the beneficiary, may sell the notes which represent the debt without removing title from the trustee, who holds it for the benefit of all parties among whom title is distributed. The trust deed is preferred to the mortgage when the debt secured amounts to a large sum, which it is desired to distribute among several creditors, each of whom advances a small part of the total debt secured by the trust deed and receives one of the notes

secured by the deed. The effect of a trust deed is the same as that of a mortgage. It differs from a mortgage only in the method of handling the transaction. The owner of the land conveys the property to the trustee to hold until the debt which it is given to secure is paid, with authority to foreclose the deed upon non-payment of the debt and distribute the proceeds among the holders of the notes.

**429. Land Contract.** When an agreement is made to purchase land, the agreement is usually evidenced by a contract, which must be in writing to conform to the requirements of the Statute of Frauds. This contract, it will be observed, contains, in addition to the essential features of the agreement, a provision that the seller is to furnish to the purchaser a complete *abstract of title* (see next section) showing a clear title in the seller, and that the purchaser is to have a certain length of time in which to examine it. When the title has been found perfect, the sale is completed by paying over the money and receiving a deed, or complying with any other provisions in the contract. It will thus be seen that one office of the land contract is to cover the period between the time of the agreement and such time as the purchaser can satisfy himself that the title is good. Another function of the land contract is to enable a purchaser to acquire a right to possession of property on a small cash payment, agreeing to pay the bulk of the purchase price at a later date, when he is to receive the deed. This kind of a contract is frequently used instead of executing a mortgage for unpaid purchase money.

One distinctive feature of land contracts is that a land contract may be specifically enforced in a court of equity if the wronged party prefers this procedure to bringing a suit for damages for its breach. The purchaser may be compelled to complete the purchase and receive the title, or the seller may be compelled to convey the land which he had agreed to sell.

### Land Contract

**This Memorandum Witnesseth,** *That Charles H. Hathaway hereby agrees to sell, and Martin F. Deale agrees to purchase at the price of Two Thousand Dollars the following described real estate, situated in Cook County, Illinois: The South East quarter* (*S.E.* ¼) *of the North West quarter* (*N.W.* ¼) *of Section twenty-nine* (29), *Township thirty-eight north* (38 *N.*),

*of Range fourteen (R. 14), East of the third principal meridian. Subject to (1) existing leases, the purchaser to be entitled to the rents, if any, from the time of delivery of Deed; (2) all taxes and assessments levied after the year 1916; (3) any unpaid special taxes or assessments levied for improvements not yet made.*

**Said Purchaser** *has paid One Hundred Dollars as earnest money, to be applied on said purchase when consummated, and agrees to pay, within five days after the title has been examined and found good, the further sum of Nine Hundred Dollars, at the office of Charles H. Hathaway, Chicago, provided a good and sufficient full covenant Warranty Deed, conveying to said purchaser a good title to said premises (subject as aforesaid B), shall then be ready for delivery. The balance to be paid as follows: One Thousand Dollars in one year, with interest from August 24th, at the rate of 6 per cent per annum, payable annually, to be secured by notes and mortgage, of even date herewith, on said premises. A complete Abstract of Title, or merchantable copy, to be furnished, within a reasonable time, with a continuation thereof brought down to this date. In case the title, upon examination, is found materially defective, within ten days after said Abstract is furnished, then, unless the material defects be cured within sixty days after written notice thereof, the said earnest money shall be refunded, and this contract to become inoperative.*

*Should said purchaser fail to perform this contract promptly on his part, at the time and in the manner herein specified, the earnest money paid as above shall, at the option of the vendor, be forfeited as liquidated damages, including commissions payable by vendor, and this contract shall be and become null and void. Time is of the essence of this contract, and of all the conditions thereof.*

**This Contract** *and earnest money shall be held by J. L. Talbot, for the mutual benefit of the parties hereto.*

**In Testimony Whereof,** *said parties hereunto set their hands, this 22d day of August, A. D.* 1916.

*CHARLES H. HATHAWAY.*
*MARTIN F. DEALE.*

**430. Abstract of Title.** This is a brief summary of the records of title relating to any particular piece of real estate. It is prepared by persons skilled in the matter, who have access to the public records, or who have a complete set of duplicate records of all property in a particular locality. Only the essential features of the history of the property and conveyances relating to it are given, generally dating back to the time when the government issued a patent to it, but if there are any defects in a conveyance, they are noted. Liens, including judgments, tax sales, and all facts of record having a bearing on the title to the property, are noted for the inspection of the examining attorney. An examination of this abstract of title will serve to disclose defects in the title to property.

**431. Guaranty Policies** are frequently issued by responsible corporations which guarantee the title to be clear up to and including a certain date, after which time additional facts of record may be made by a continuation of the abstract. These policies are of value in assuring purchasers of the chain of title, and against any possible remote claim which may be raised. They also serve to simplify the matter of examination of abstracts, and relieve the buyer from anxiety concerning errors and oversights which the average attorney may make in inspecting a title. They are in common use in the larger cities.

## CHAPTER XLVIII

## REAL ESTATE CONVEYANCES — Continued

### LEASES

**432. Landlord and Tenant.** The relation of landlord and tenant is created by an agreement wherein the landlord conveys an interest in real estate, which interest is less than a freehold estate, to another person, called the tenant, who is to use and hold the land, building, or room for a term of years. This agreement is called a lease and may be made orally or in writing, though most states now provide that all leases for a period longer than one year must be in writing. The compensation, whether in money or produce, is called the rent.

**433. Kinds of Tenancies.** The principal classes of tenancies are *estates for years*, *tenancies from year to year*, *tenancies at will*, and *tenancies at sufferance*. A lease for a definite time, as six months, two years, or ninety-nine years, conveys a *tenancy for years*. If after the term of the lease expires, the tenant continues to occupy the premises without objection from the landlord, he has a tenancy from *year to year*, (or *month to month*, depending on the term of his original lease) and his duties continue to be the same as they were under the written lease. He can only be removed from possession at the end of a year, or month, as the case may be. A tenancy which may be terminated by either party at pleasure is a tenancy *at will*, while a tenancy *at sufferance* exists when one who has originally come into possession of land lawfully holds possession without right or permission by the landlord after the expiration of his term.

Since these various tenancies are regulated by statutes or judicial decision, the student should consult the particular laws of his own state when questions arise as to their termination or creation.

**434. A Lease** is a contract for an interest in lands, and as previously noted is generally required to be in writing when made

## LEASE

**This Indenture,** MADE this first day of January A. D. 19— BETWEEN J. B. Olmstead — 734 Mokadnock Bldg. Chicago party of the first part, and D. B. Stewart 356 Sheridan Road, Chicago party of the second part.

**Witnesseth,** That the party of the first part, in consideration of the covenants of the party of the second part, hereinafter set forth, ~~does~~ by these Presents, lease to the party of the second part, the following described property, to-wit: The building located at 347 Adams St., Chicago, in the County of Cook and State of Illinois

**To Have and to Hold the Same** To the party of the second part, from the first day of January, 190—, to the thirty-first day of December, 190—. And the party of the second part, in consideration of the leasing the premises as above set forth, covenants and agrees with the party of the first part to pay the party of the first part, at the office of the party of the first part rent for the same, the sum of Fifteen Hundred $—— Dollars, payable as follows, to-wit: Monthly in advance, in payments of one hundred twenty-five dollars each, on the first day of each and every month during the term of this lease.

**And the Party of the Second Part** Covenants with the party of the first part, that at the expiration of the term of this lease he will yield up the premises to the party of the first part, without further notice, in as good condition as when the same were entered upon by the party of the second part, loss by fire or inevitable accident and ordinary wear excepted.

**It is Further Agreed** By the party of the second part, that neither he nor his legal representatives will underlet said premises or any part thereof, or assign this lease without the written assent of the party of the first part first had thereto.

**And it is Further Expressly Agreed** Between the parties hereto, that if default shall be made in the payment of the rent above reserved, or any part thereof, or any of the covenants or agreements herein contained to be kept by the party of the second part, it shall be lawful for the party of the first part or his legal representatives, into and upon said premises or any part thereof, either with or without process of law, to re-enter and re-possess the same at the election of the party of the first part, and to distrain for any rent that may be due thereon upon any property belonging to the party of the second part. And in order to enforce a forfeiture for non-payment of rent it shall not be necessary to make a demand on the same day the rent shall become due, but a failure to pay the same at the place aforesaid or a demand and a refusal to pay on the same day, or at any time on any subsequent day, shall be sufficient; and after such default shall be made, the party of the second part and all persons in possession under him shall be deemed guilty of a forcible detainer of said premises under the statute.

**And it is Further Covenanted and Agreed** Between the parties aforesaid that the said party of the second part shall pay all bills for waters, gas and electric light that may become due on the building herein leased during the term of this lease.

The covenants herein shall extend to and be binding upon the heirs, executors and administrators of the parties to this Lease.

**Witness the Hands and Seals** Of the parties aforesaid, the day and year first above written.

J. B. Olmstead Seal

D. B. Stewart Seal

for a period longer than one year. In some states, by statute, this limit is extended to three years. By common law the lease need not be sealed; but if by statute it must be recorded, it is required to be both sealed and acknowledged. In order to protect the tenant in the enjoyment of a long lease many states require it to be recorded. In Connecticut, Mississippi, Oregon, Rhode Island, South Carolina, Tennessee, and Vermont, if leases are given for more than one year, they should be recorded. In Maine, Maryland, Massachusetts, and New Hampshire, leases for seven years or longer should be recorded. In Texas all leases should be recorded. The lease should be signed by both parties, and it should be made in duplicate, each party retaining a copy.

**435. Parts of a Lease.** The words usually used in the granting clause are "demise and lease," but these exact words are not necessary. The premises should be so described that they can be identified with certainty. The length of the lease is usually a matter of agreement, and may be as long as the parties choose, except that the landlord cannot grant a greater estate than he owns. In large cities a lease for ninety-nine years, or even longer, is not an uncommon thing. In such leases, the rental is usually agreed upon for a shorter term of years; and at the end of this time a revaluation of the property is made according to some plan agreed upon in the contract, and the amount of the rental for the next period determined. Such leasehold interests are often very valuable, because the price of real estate may rise considerably before the time of revaluation comes around.

**436. The Rent.** The amount of rent is usually agreed upon in advance, but it may be left for future determination according to some agreed plan. It may be a gross sum in advance, a monthly sum, or a certain share in the crops to be raised during the term of the lease. When a monthly rent is named, the tenant, in the absence of a special agreement, has until the last of the month to make payment. When nothing is said about the place of payment, it is sufficient if tendered on the premises.

**437. Landlord's Covenants.** The covenants which the landlord usually makes in a lease include guarantees to give the tenant quiet enjoyment of the property and protection against mort-

gages and other incumbrances, to make necessary repairs, and to pay taxes and assessments. There may be other covenants peculiar to special cases. The covenant of quiet enjoyment is implied, and exists whether it is stated or not. Under it the landlord is bound not to do any act, nor to permit any which will materially affect the rights of the tenant in the quiet enjoyment of his holding. Any material interference with the tenant's right to the beneficial enjoyment of the premises, will amount to an eviction in law, which will justify the tenant in declaring the term at an end, and in refusing to be further bound by the terms of the lease. Without a covenant for protection against incumbrances, if the tenant should be evicted by a mortgagee, he would lose all his rights under the lease. With the covenant, he may sue the landlord for any damages or losses which are the consequence of his eviction.

The covenant to repair can never rest upon mere implication, for the common law, with regard to expenses of this kind, presumes so strongly against the tenant, that even though the premises should be burned to the ground, he must continue to pay rent, unless there is an express covenant to the contrary in his lease, and yet he is given no power to compel his landlord to rebuild the structure destroyed. But by statute and precedent this rule has been very generally set aside. The custom very commonly prevails of inserting a clause in all written leases providing for the suspension of rent "in case of fire or other unavoidable casualty"; and that the "landlord may at his option terminate the lease, or repair the premises within thirty days, and failing to do so, the term hereby created shall cease and determine." If the house is dilapidated and disfigured as to paint and paper, locks and blinds, the tenant cannot demand their repair, in the absence of express agreement. It is therefore important for the tenant to ascertain the condition of the premises before taking possession, and to obtain a specific agreement as to the making of repairs. In tenements or apartments where several tenants occupy various portions of the premises, the landlord must keep the roof, basement, halls, entrances, walks, and yard in repair, as the tenants do not individually control them, and they are intended for common use. When the landlord covenants to repair and fails to do so, the tenant is seldom justified in refusing to pay

rent, but is limited to a right of action against the landlord for breach of the covenant. A covenant to renew the lease gives the option to the tenant either to vacate or remain upon the premises at the end of the term. The covenant on the part of the tenant to pay rent is generally implied and if no stated sum is specified the reasonable rental value is recoverable against him.

**438. Tenant's Covenants.** The tenant may also agree to do any of a number of acts, the most usual covenants being covenants to repair; to pay rent, taxes, and assessments; not to assign the lease; to use the premises only for certain agreed purposes, or in a particular manner; and to redeliver the premises at the termination of the period in good condition and repair, loss by fire and ordinary wear being generally excepted. As is true with the landlord's covenants, the tenant's covenants may vary to suit the circumstances of the particular lease. In the absence of any agreement as to repair, the duty is imposed upon the tenant to make repairs, but he need not make good the ordinary wear and tear naturally incident to the use of the premises for the purpose for which they were leased. Waste, or the destruction of the premises, whether by his will or his permission or his carelessness is, of course, not tolerated.

The payment of rent according to agreement scarcely needs a covenant on the part of the tenant, as it will be implied, and will not ordinarily be excused. Though fire or flood may have made the premises uninhabitable, yet unless the tenant has protected himself by suitable stipulations to the contrary, or a local statute has changed the rule of the common law, he must pay his rent.

When the agreement is that the tenant is to pay the taxes and insurance, the lease should so state, for otherwise the duty is upon the landlord. Likewise, when the tenant is not to have the right to assign his lease, or sublet the premises, the provision should be in the lease, for at common law the tenant has such rights, though he cannot escape a personal liability to his landlord for the payment of the rent by assigning the lease to another. Modern leases usually contain covenants against sub-letting or assigning, for the landlord generally desires to select his own tenants.

If the tenant covenants "to return and redeliver the premises at the end of the term, in good order and condition, reasonable wear and tear only excepted," he is bound under this agreement to rebuild a house, if it be burned down during the lease. For this reason, modern leases often add to the above exception, "damage by fire and other unavoidable accidents also excepted," or "damage by the elements and acts of God excepted." These have the effect of relieving the tenant from the necessity of rebuilding.

**439. Tenants' Fixtures.** There are some improvements a tenant may add during his term which he may take away with him at the termination of his lease. The general rule applicable to fixtures is that, as between heir and executor, vendor and purchaser, mortgagor and mortgagee, debtor and creditor, if personal property be annexed to the realty, it becomes a fixture, so that one who takes the property, or has a lien upon it for a debt, will get the benefit of the improvement. As between landlord and tenant, however, the modern doctrine is more favorable to the tenant, and allows him to remove all articles of personal property annexed to the real estate for purpose of trade, agriculture, or domestic use and convenience, when such removal will not result in serious or permanent injury to the realty.

The method of affixing is often important in determining this question. Thus, if the articles are fastened with screws this may serve as evidence of an intention to later remove them and may prevent them from becoming fixtures. Among articles held to be removable by tenants in some of the cases that have come before the courts are: Stoves, pumps, gates, looking glasses, stables on blocks, gas fixtures, hop-poles, machinery fastened with screws to the floor, and similar articles of trade, agricultural, or domestic use. Among those held not removable are: Barns built upon foundations set in the ground, trees, hedges, windows, locks and keys. Each question must be decided upon its own particular facts, for the great determining factor always is the intention of the parties, as evidenced by their acts, at the time of annexing the article to the freehold.

**440. Notice to Quit.** One of the ways in which a tenancy may be terminated is by a notice to quit, given in a regular

manner and under suitable circumstances. If one holds a lease for years, he is not entitled to a notice to quit at the expiration of the term, unless a statutory provision requires it, for he has no right to remain longer. But if, as frequently happens, the landlord consents to the tenant's holding over after his term, and the tenant thereby becomes a tenant from year to year, month to month, or for whatever period rent is paid, the tenant must be served with a proper and timely notice to quit the premises before he can be ejected by a suit. The notice need not be formal, but it should specify the particular day when the tenant is required to quit, and it must be written. The length of time allowed the tenant in which to move is very important, and is largely governed by statutory regulations, which should always be consulted. In general, the notice to quit should be given one full rental period before the expiration of the lease, unless the eviction be for the non-payment of rent, when a much shorter period is usually provided. The right of notice also applies as against the landlord, and the tenant from year to year as well as the landlord may terminate the lease by a proper notice.

# INDEX


Abstract of title, 365.
Acceptance, 32; communication of, 34; of draft, 106; implied, 106; for honor, 107; virtual, 107; effect of, 107; qualified, 107; form of, 110; presentment for, 144.
Accepted draft, 144.
Accommodation note, 122.
Accord and satisfaction, 74.
Act of God, 242.
Active partner, 278.
Agency, 248-274; defined, 249; general, 249; termination of, 263; dissolution of, 271, 273.
Agent, 249; right to contract, 28; right to compensation, 262, 264; to indemnity, 264; to protection, 265; of corporation, 311.
Agreement, mutuality of, 30; essentials of, 30-39.
Alien enemy, act of, 242.
Aliens and alien enemies, 27.
Alteration, of instrument, 58, 173; and forgery, 131.
Annual interest, 161.
Anticipatory breach, 65.
Apparent consideration, 42.
Articles, of partnership, 279; of incorporation, 308.
Ascertained goods, 192.
Assignment, of contracts, 87; inadequacy of, 93; of stock certificates, 304; of insurance policies, 324; of insurance, 331; of mortgage, 360.
Attachment, 72.

Bailed property, redelivery of, 223.
Bailee, 205; diligence required of, 221; right to use, 222; remedies of, 228.
Bailments, 218-224; defined, 218; kinds of, 219; benefit of bailor, 220; benefit of bailee, 225; mutual benefit, 227; for performance of services, 233; exceptional, 238-247.
Bailor, liability of, 232.
Baggage, 246.
Bank draft, 116.
Bankruptcy, 59.
Bearer, paper payable to, 135.
Beneficiary, 330.
Benefit received, 40.
Bill of exchange, 97.
Bill of sale, 188.
Bills of lading, 201; negotiable, 204.
Bona fide holder, 127.
Borrower, liability of, 226; rights of, 226.
Breach, of contract, 62; of warranty, remedies for, 216.
Burglary insurance, 335.
Buyer, remedies of, 215.

Capital stock, 304; classes of, 307.
Casualty insurance, 334.
Caveat emptor, 209.
Certificate, of deposit, 116; of protest, 155; of stock, 304.
Charter, of corporation, 297, 302.
Chattel mortgage, 198.
Check, 97; defined, 112; form of, 113; certified, 114, 115; cashier's, 115; bank check, 116; canceled, 117.
Civil law, 5.
C.O.D. shipment, 194.
Collateral note, 124.
Collection, guaranty for, 170.
Commercial law, 6.
Common carrier, of goods, 240; of passengers, 244; rights of, 245.

Common law, 3.
Common stock, 307.
Compound interest, 160.
Concurrent condition, 53.
Conditional liability, 148.
Conditional offer, 32.
Conditional sales, 197.
Conditions in contracts, 53.
Co-maker, 167.
Connecticut rule, partial payments, 164.
Consideration, defined, 40; sufficiency of, for simple contracts, 40-44; for formal contracts, 44; for negotiable paper, 130.
Constitutional law, 2.
Contingent interest, 342.
Continuing guaranty, 171.
Contract, defined, 12; validity of, 13; solemnity of, 14; under seal, 15; parol, 16; express and implied, 16; executed and executory, 17; joint, several, and joint and several, 18; death of joint contractor, 19; discharge of, 52-68; assignment of, 87; form of, 89; to sell, 179; form of, 184-190.
Contribution, right of, 171.
Conveyances of real estate, 347-373.
Corporations, 296-317; right to contract, 28; defined, 297; nature of, 298; kinds of, 299; compared with partnerships, 299; formation of, 300; property of, 301; charter of, 302; capital of, 303; capital stock of, 304; powers of, 310; officers of, 311; de facto, 314; dissolution of 315; foreign, 316.
Courts of law, 5; of equity, 5; of record, 70.
Counterclaim, 82.
Covenants, and warranties, 354; of landlord, 369; of tenant, 371.
Credit insurance, 335.
Creditors' rights, 196; against partners, 285; of corporations, 313.
Criminal acts, contracts to do, 50.
Criminal law, 5.
Crops, sale of, 185.
Curtesy, 340.

Damages, 62, 65, 213.
Death of joint contractor, 19; of joint guarantor, 174.
Deeds, 347.
Defeasance clause, 358.
Defenses, 130; personal, 132.
Degrees of care, 219.
Delivery, 101, 135; to buyer, 195; sufficiency of, 197.
Demand draft, 109.
Deposit, 220.
Detriment suffered, 41.
Directors of corporation, 311.
Disabilities, 21.
Discharge of contracts by performance, 52; by payment, 55; by tender, 55; by impossibility, 56; by agreement, 57; by operation of law, 58; by death, 60; by breach, 62-66; of indorsers, 154.
Dishonor, 148.
Dissolution of partnership, 288-295; of corporation, 315.
Diversion, 173.
Divisible contract, 63.
Documents of title, 203.
Dormant partner, 279.
Dower, 340.
Draft, 97; 104-111; transfer, 109; sight, 109; demand, 109, 153; time, 110; accepted, 144.
Due course, 126.
Duress, 37.

Easements, 343.
Eminent domain, 343.
Employer's liability, 265; liability insurance, 334.
Endowment insurance, 329.
Equity of redemption, 360, 362.
Escheat, 343.

Estate, an, 338; life, 339; for years, 341; future, 342.
Executed and executory contracts, 17.
Execution, 71.
Exemptions, 71.
Expectancy, 9.
Express contract, 16.

Failure of consideration, 43, 132.
Fee, simple. 338.
Fidelity insurance, 335.
Fire insurance, 321.
Fixtures, 372.
Forgery, 131.
Formal contracts, 44.
Franchise of corporation, 297.
Fraud, 37, 215; contracts induced by, 49; statute of, 75; in the transaction, 132; on surety, 172.

Garnishment, 71.
Goods, wares, and merchandise, 184.
Gratuitous loans, 225.
Guaranty, defined, 167; contract of, 168; kinds of, 170; continuing, 171; not negotiable, 174; validity of, 175; and suretyship, 167-177; policies, 366.
Guarantor, 167; liability of, 169; rights of, 172; discharge of, 174.
Guests, 238.

Habendum et tenendum, 354.
Hire, by bailee, 231; by bailor, 233; for safe-keeping, 235; for transportation, 236.
Holder in due course, 126-134.
Holidays, 153.
Homestead, 341.

Illegal acts, contracts to do, 50.
Illegality of consideration, 133.
Immoral acts, contracts to do, 49.
Implied contracts, 16.
Implied acceptance, 106.
Impossibility, 56.
Incapacity of a party, 131.
Incontestable insurance, 333.
Indemnity, right of, 171.
Indorsement, kinds of, 137; effect of, 138; in full, 139; in blank, 139; restrictive, 140; qualified, 140; conditional, 140.
Indorsers, contract of, 141, 167; may become surety, 174; irregular, 141.
Infants, 24.
Injunction, 6, 73.
Inn-keeper, 238.
Innocent holder, 127.
Insane persons, 22.
Insurable interests, 322, 330.
Insurance, 320-336.
Insured, 322, 330.
Insurer, 322, 330.
Intention to contract, 30.
Interest, defined, 160; when payable, 161; rate of, 162; on accounts, 162; on partial payments, 163.
Intoxicated persons, 23.

Joint and several contract, 18.
Joint contract, 18.
Joint stock companies, 318-319; defined, 318; discussed, 318-319.
Joint tenancy, 10, 345.
Judgment, 70; note, 123.

Lack of consideration, 132.
Land contract, 364.
Landlord, 367.
Law, defined, 1; municipal, 2; kinds of, 2; constitutional, 2; statute, 3; common, 3; order of precedence, 4; courts of, 5; civil and criminal, 5; suit at, 5; commercial, 6.
Lease, 367.
Legal incapacity, 24.
Legal interest, 161.
Legal tender, 56.
Lender, liability of, 226; bailee's right of, 234.
Levy, 71.
Liability, of common carrier, 242, 245; of employer, 265.
Lien, seller's right of, 213; of agent, 264.

Life insurance, 329-333.
Limitations, statute of, 79.
Limited partner, 279.
Limited payment life, 329.
Liquidation of assets, 315.
Loss or detriment suffered, 41.
Loss, proof and recovery of, 325.

Mandate, 220.
Marine insurance, 321.
Married women, 27.
Maturity of paper 130.
Mental incapability, 21.
Merchants' rule, 164.
Merger, 58.
Mistake of fact, 35.
Mortgage, 198; real estate, 358.
Mortgagee, 198.
Mortgagor, 198.
Municipal law, 2.
Mutual promises, 42.

Necessities, infants' liability for, 26.
Negotiable bills of lading, 204.
Negotiable instruments, 93-103; defined, 96.
Negotiability, 95.
Note, 97; defined, 119; form of, 120; joint and several, 120; accommodation, 122; incomplete, 122; judgment, 123.
Notice, of dishonor, 148, 156; of protest, 156; of dissolution of partnership, 293; to quit, 373.
Novation, 57.

Offer, 31; communication of, 31.
Open policy, 321.
Options, 44.
Ostensible partner, 278.

Parol evidence rule, 85; contracts by, 16.
Part payment, 189.
Partial payments, 163.
Parties, defined, 21; competency of, 21-29.
Partners, kinds of, 278; authority of, 282; relations between, 283.
Partnership, 275-295; defined, 275; essentials of, 276; creation of, 277; articles of, 279; dissolution of, 288-295; limited, 293.
Pawn, 227.
Payment, 55; guaranty for, 170.
Personal accident insurance, 334.
Personal property, 7.
Place of presentment, 146, 152.
Plate glass insurance, 335.
Pleadings, 69.
Pledge, 227.
Police power, 343.
Policy, of fire insurance, 320; of life insurance, 329.
Post-dating, 117.
Post office department, 246.
Potential existence, 181.
Power of attorney, 123.
Precedent condition, 53.
Preferred stock, 307.
Premium of insurance, 320.
Presentment, for acceptance, 144-150; for payment, 151-159; of checks, 153; manner of, 154.
Price, 181.
Principal, 249; duties to agent, 262; to third persons, 265; disclosed and undisclosed, 266; responsibility of, 267.
Prior party, payment to, 133.
Promissory note, 97, 119.
Property, defined, 7; real and personal, 7; in possession and in action, 9; in expectancy, 9; how held, 10; real, 337; how held, 344.
Protest, 155.
Public justice, contracts obstructive of, 49.
Public policy, subject matter contrary to, 48.

Quitclaim deed, 356.

Real estate, 337-346; conveyances of, 347-373.
Real property, 7.

Reasonable time for holding check, 153.
Recording of deed, 351; of mortgages, 362.
Recovery of price, 212; of damages, 213.
Reddendum, 354.
Registration of land, Torrens system, 352.
Release deed, 363.
Remainder, 342, 345.
Remedies, 69-73; of seller, 212; of buyer, 212; for breach of warranty, 216; of mortgagee, 361.
Rent, amount of, 369.
Replevin, 72.
Representations in insurance, 323, 332.
Resale, right of, 214.
Rescinding of sale, 214.
Restraint, of trade, 48; of marriage, 48.
Reversion, 342, 345.
Revival of outlawed claims, 81.
Revocation by surety or guarantor, 175.
Rules of evidence, 85.

Sales, of personal property, 178-183; at a valuation, 182; determining of value, 186; bill of, 188; conditional, 197; of mortgage, 360.
Saving clauses, 81.
Seal, 15.
Second mortgage, 361.
Securities, parting with, 174.
Servant, 249.
Set-off and counterclaim, 82, 133.
Several contract, 18.
Severalty, 10.
Sight draft, 109.
Simple interest, 160; always presumed, 161.
Special defenses, 74.
Specific performance, 64, 73.
Spendthrifts, 24.
Statute, of frauds, 75, 184; of limitations, 79.
Statute law, 3.
Stockholders, 312.
Stock subscription, 309.
Stoppage in transit, 213.
Straight life insurance, 329.
Subject matter, defined, 47; what is not valid, 47-51.
Subrogation, right of, 172.
Subsequent condition, 53.
Subsequent purchaser, 195.
Subsidiary terms, breach of, 63.
Substantial performance, 54.
Suit at law, 5.
Summons, 69.
Surety, 167; liability of, 168; rights of, 171; discharge of, 172.
Suretyship, defined, 167.
Survival of contract, 19.

Telegraph and telephone companies, 246.
Tenancy, joint and several, 10; in common, 10, 346; joint, 345; for term of years, 346; in trust, 346.
Tenancies, kinds of, 367.
Tenant, 367.
Tender, 55.
Things in possession, 9; in action, 9.
Third persons, rights of, in contract, 43; in agency, 269.
Timber, sale of, 185.
Time, of performance, 54; of presentment, 146, 151.
Title, transfer of, 191-199; to C.O.D. shipments, 194; guaranty insurance, 334; abstract of, 365.
Torrens Registration, 352.
Transactions with persons now deceased, proof of, 86.
Transfer, to innocent holder, 127; without indorsement, 135; by indorsement and delivery, 136; of title, 191-199; by bills of lading, 200; by documents of title, 203.

Trial, 70.
True owner, surrender to, 228.
Trust deed, 363.
Trust estate, 346.

Unascertained goods, 194.
Unauthorized acts of corporations, 314.
Undue influence, 38.
Unreal mutual assent, 35.
U. S. Rule partial payments, 163.
Usury, 164.

Validity of contracts, 13.
Valued policy, 321.
Vested interest, 342.
Void instruments, 131.
Voidable contracts of infants, 24.

Waiver, 57; of presentment, 154; of notice, 156.
Warranties, 207-211; defined, 207; express, 207; implied, 207; of title, 209; remedies for breach of, 216; in insurance, 323, 332; of real estate, 354.
Warranty deed, 353; special, 355.
Withdrawal of offer, 35.
Writing, what constitutes, 187.

# APPENDIX

## TABLE OF LIMITATIONS

This table shows the time limit, in years, for bringing actions on different classes of contracts.

| STATES | Open Accounts | Contracts in Writing | Judgments | STATES | Open Accounts | Contracts in Writing | Judgments |
|---|---|---|---|---|---|---|---|
| Alabama | 3 | 6*j* | 20*a* | Montana | 5 | 8 | 10*k* |
| Alaska | 6 | 6*j* | 10 | Nebraska | 4 | 5 | 5 |
| Arizona | 4*b* | 4 | 5 | Nevada | 4*l* | 6*l* | 6 |
| Arkansas | 3 | 5 | 10 | New Hampshire | 6 | 6*m* | 20 |
| California | 2–4 | 4*c* | 5 | New Jersey | 6 | 6 | 20 |
| Colorado | 6 | 6 | 6*d* | New Mexico | 4 | 6 | 7 |
| Connecticut | 6 | 6 | .... | New York | 6 | 6 | 20*n* |
| Delaware | 3 | 6*i* | 20 | North Carolina | 3 | 3*j* | 10*o* |
| District of Columbia | 3 | 3*h* | .... | North Dakota | 6 | 6 | 10 |
| Florida | 2 | 5*i* | 20 | Ohio | 6 | 15 | 21*p* |
| Georgia | 4 | 6*i* | 7 | Oklahoma | 3 | 5 | 5 |
| Idaho | 4 | 5 | 6 | Oregon | 6 | 6*j* | 10 |
| Illinois | 5 | 10 | 20*e* | Pennsylvania | 6 | 6*i* | 20 |
| Indiana | 6 | 10 | 20 | Rhode Island | 6 | 6 | 20 |
| Iowa | 5 | 10 | 20*f* | South Carolina | 6 | 6 | 20 |
| Kansas | 3 | 5 | 5 | South Dakota | 6 | 6*i* | 20*f* |
| Kentucky | 5*g* | 5 | 15 | Tennessee | 6 | 6 | 10 |
| Louisiana | 3 | 5 | 10 | Texas | 2 | 4 | 10 |
| Maine | 6 | 6 | 20 | Utah | 4 | 6 | 8 |
| Maryland | 3 | 3*h* | 12 | Vermont | 6 | 6 | 8 |
| Massachusetts | 6 | 6*i* | 20 | Virginia | 2–5 | 5*j* | 10*q* |
| Michigan | 6 | 6*j* | 10 | Washington | 3 | 6 | 6 |
| Minnesota | 6 | 6 | 10 | West Virginia | 5 | 10 | 10 |
| Mississippi | 3 | 6 | 7 | Wisconsin | 6 | 6*i* | 20*a* |
| Missouri | 5 | 10 | 10 | Wyoming | 8 | 10 | 10 |

(*a*) J. P. judgment 6 yr. (*b*) 3 yr. unless both parties are merchants. (*c*) 2 yr. if executed outside of state. (*d*) 20 yr. on judgments rendered in Court of Record. (*e*) J. P. judgment 10 yr. (*f*) 10 yr. if not in Court of Record in state. (*g*) 5 yr. if between merchants. (*h*) 12 yr. if under seal. (*i*) 20 yr. if under seal. (*j*) 10 yr. if under seal. (*k*) J. P. Courts 5 yr. (*l*) 2 yr. if incurred out of state. (*m*) 20 yr. on mortgage. (*n*) Inferior courts 6 yr. (*o*) 7 yr. if not in Court of Record. (*p*) May be kept alive indefinitely alive by execution once in five years. (*q*) 20 yr. if execution made and returned.

The following table shows the rates of interest and penalties for usury in the several states.

| States and Territories | Legal Rate | Highest Rate Allowed | Penalty for Usury |
|---|---|---|---|
| Alabama | 8% | 8% | Forfeiture of all interest. |
| Alaska | 8% | 12% | Loss of interest if uncollected; forfeiture of double the interest if collected. |
| Arizona | 6% | 12% | Same as Alaska. |
| Arkansas | 6% | 10% | Forfeiture of principal and interest. |
| California | 7% | any | None. |
| Colorado | 8% | any | None. |
| Connecticut | 6% | 12% | Forfeiture of principal and interest; fine. |
| Delaware | 6% | 6% | Forfeiture of sum equal to amt. loaned. |
| Dist. of Columbia | 6% | 6% | Forfeiture of all interest. |
| Florida | 8% | 10% | Forfeiture of all interest. |
| Georgia | 7% | 8% | Forfeiture of excess of interest. |
| Hawaii | 8% | 12% | Forfeiture of excess of interest. |
| Idaho | 7% | 12% | Forfeiture to debtor of balance due and to state 10% per year on contract. |
| Illinois | 5% | 7% | Forfeiture of all interest. |
| Indiana | 6% | 8% | Forfeiture of excess of interest over 6%. |
| Iowa | 6% | 8% | Forfeiture of interest and costs; debtor pays 8% to school fund. |
| Kansas | 6% | 10% | Forfeiture of double the excess over 10%. |
| Kentucky | 6% | 6% | Forfeiture of excess of interest. |
| Louisiana | 5% | 8% | Forfeiture of all interest. |
| Maine | 6% | any | None. |
| Maryland | 6% | 6% | Forfeiture of excess of interest. |
| Massachusetts | 6% | any | Forfeiture of all over 18% on loans under $1,000. |
| Michigan | 5% | 7% | Forfeiture of all interest. |
| Minnesota | 6% | 10% | Forfeiture of interest. |
| Mississippi | 6% | 8% | Forfeiture of interest. |
| Missouri | 6% | 8% | Forfeiture of all interest and security. |
| Montana | 8% | any | None. |
| Nebraska | 7% | 10% | Forfeiture of all interest. |
| Nevada | 7% | any | None. |
| New Hampshire | 6% | 6% | Forfeiture of three times the excess of interest. |
| New Jersey | 6% | 6% | Forfeiture of all interest and costs. |
| New Mexico | 6% | 12% | Forfeiture of double excess; fine. |

| States and Territories | Legal Rate | Highest Rate Allowed | Penalty for Usury |
|---|---|---|---|
| New York | 6% | 6% | Forfeiture of principal and interest. |
| North Carolina | 6% | 6% | Forfeiture of double the amount of interest. |
| North Dakota | 7% | 12% | Forfeiture of all interest. |
| Ohio | 6% | 8% | Forfeiture of excess of interest over 8%. |
| Oklahoma | 6% | 10% | Forfeiture of all interest. |
| Oregon | 6% | 10% | Forfeiture of interest and principal. |
| Pennsylvania | 6% | 6% | Forfeiture of excess of interest. |
| Philippine Islands | 6% | any | |
| Porto Rico | 6% | 12% | Loss of entire interest. |
| Rhode Island | 6% | any | None. |
| South Carolina | 7% | 8% | Forfeiture of all interest. |
| South Dakota | 7% | 12% | Forfeiture of all interest; also a misdemeanor. |
| Tennessee | 6% | 6% | Forfeiture of principal and interest if in writing; otherwise, forfeiture of interest. |
| Texas | 6% | 10% | Forfeiture of all interest. |
| Utah | 8% | 12% | Forfeiture of principal and interest. |
| Vermont | 6% | 6% | Forfeiture of excess of interest. |
| Virginia | 6% | 6% | Forfeiture of all interest. |
| Washington | 6% | 12% | Loss of interest if uncollected; forfeiture of double interest if collected. |
| West Virginia | 6% | 6% | Forfeiture of excess of interest. |
| Wisconsin | 6% | 10% | Loss of all interest; forfeiture of treble interest if collected. |
| Wyoming | 8% | 12% | Forfeiture of interest. |

## EXEMPTIONS

In most states debtors are protected by laws which exempt certain property from seizure by creditors. The property so exempt usually includes homestead, personal property specified as to kind or value or both, and part or all of the wages of the debtor for a specified period. Homestead and other exemption laws can usually be waived by special agreement and exemptions are generally not valid as against the purchase price of the property exempted. In some states exemptions are not valid against properly recorded mortgages, even in the absence of waiver. The following list of exemptions by states is as nearly correct as these can be stated in abbreviated form. The statutes of the various states should be consulted for exact statements of details.

**Alabama** — Homestead, house and lot in city or 160 acres in country; must not exceed $2000. Personal property, $1000 and specified items. Wages, $25 a month.

**Alaska** —Homestead, ¼ acre in city or 160 acres in country; must not exceed $2500. Personal property, specified items with various limits of value. Earnings for 60 days preceding levy when necessary for the support of family.

**Arizona** — Homestead, $4000; claim must be recorded. Personal property, specified items with various limits of value. Half of earnings for 30 days preceding levy.

**Arkansas** — Homestead, 1 acre in city, 160 acres in country, not exceeding $2500 in value; or ¼ acre in city or 80 acres in country, any value. Personal property, married man $500; single man $200 and wearing apparel. Laborer's wages for 60 days preceding levy.

**California** — Homestead, $5000. Personal property, specified items in varying amounts. Wages for 30 days if necessary for support of family. ½ of wages is liable for debts for necessities.

**Colorado** — Homestead, $2000; claim must be recorded. Personal property, specified items in varying amounts. 60% of wages. All wages if $5 per week or less.

**Connecticut** — Homestead, $1000; claim must be recorded. Personal property, specified items in varying amounts. Wages, $50.

**Delaware** — Homestead, none. Each county has a special law for exemptions of personal property.

**District of Columbia** — Personal property, specified items in varying amounts. Wages for 2 months preceding levy, not to exceed $100 per month.

**Florida** — Homestead, ½ acre in city, 160 acres in country. Personal property, $1000 to heads of families residing in the state. All wages.

**Georgia** — Homestead, the state constitution allows $1600 realty or personalty, or both; the statutes allow 50 acres of land and five acres additional for every child under 16. Personal property, specified items. All laborers' wages.

**Idaho** — Homestead, $5000 for head of family; $1000 for single person. Personal property, specified items. Wages for 30 days.

**Illinois** — Homestead, $1000. Personal property, married, $400; single, $100. Wages, $15 a week for head of family.

**Indiana** — Homestead, $600, real or personal property, or both, to resident householders and resident married women. 1 month's wages, not exceeding $25.

**Iowa** — Homestead, ½ acre in city, 40 acres in country, or any size if less than $500 in value. Personal property, specified items in varying amounts. Wages for 90 days.

**Kansas** — Homestead, 1 acre in city, 160 acres in country. Personal property, specified items. Wages for 3 months preceding levy.

**Kentucky** — Homestead, $1000. Personal property, specified items. Wages 90% if $75 per month or less; $67.50 if more than $75 per month.

**Louisiana** — Homestead, $2000 if not over 160 acres; claim must be registered. Personal property, specified items. All wages of laborers.

**Maine** — Homestead, $500; must be recorded. Personal property, specified items. Wages, $20, not good as against debts for necessities.

**Maryland** — Personal property, $100. Wages to the amount of $100. Attachment does not reach wages accruing after date of levy.

**Massachusetts** — Homestead, $800; claim must be recorded. Personal property, specified items. Wages, $20; only $10 against debts for necessities.

**Michigan** — Homestead, $1,500; must not exceed 1 lot in city or 40 acres in country. Personal property, specified items in varying amounts. Household goods, $250. Stock in trade, $250. Wages, householder, $8 to $30; single man, $4 to $15.

**Minnesota** — Homestead, 1 lot in city, ½ acre in town, 80 acres in country. Homestead not allowed single men unless they actually reside on the lot. Personal property, specified items in varying amounts. Wages for 30 days preceding levy, not exceeding $35.

**Mississippi** — Homestead, $2,000; if in the country must not exceed 160 acres; may be increased to $3000 by filing homestead declaration. Personal property, specified items in varying amounts. Wages, $50 per month to head of family, except when due for board and lodging.

**Missouri** — Homestead, $3000 in city; $1500 in country and small towns. Personal property, specified items and $300 in personal property or real estate. 90% of wages for 30 days.

**Montana** — Homestead, $2500. Not to exceed ¼ acre in city or 160 acres in country. Personal property, specified items. Wages for 45 days.

**Nebraska** — Homestead, $2000; not to exceed 2 lots in city or 160 acres in country. Personal property, specified items; also $500, if debtor has no land. 90% of wages of head of family.

**Nevada** — Homestead, $5000. Personal property, specified items. Wages not exceeding $50 earned in calendar month during which process issues.

**New Hampshire** — Homestead, $500. Personal property, specified items. Wages, $20, not good as against debts for necessaries.

**New Jersey** — Homestead, $1000 if advertised and recorded. Personal property, $200 and wearing apparel. All wages.

**New Mexico** — Homestead, $1000. Personal property, specified items. Wages for 3 months except for necessaries.

**New York** — Homestead, $1000, provided deed creating the estate states that property is to be held as a homestead. Personal property, certain specified items and $250 worth in addition. Wages of self and minor children for 60 days if necessary for support of family.

**North Carolina** — Homestead, $1000. Personal property, $500. Wages for 60 days if necessary for support of debtor's family.

**North Dakota** — Homestead, $5000; if widow or widower occupy premises the same. Personal property, specified items. Wages, none.

**Ohio** — Homestead, $1000, $500 in lieu of homestead. Personal property, specified items. Wages, personal earnings of self and minor children earned within 3 months if necessary for support of family. If debt is for "necessaries," 10% of personal earnings is not exempt.

**Oklahoma** — Homestead, 1 acre in city or town, 160 acres in country, including improvements to $5000. Personal property, specified items. "Current wages for 90 days" to head of family.

**Oregon** — Homestead, $1500, but in no instance less than 1 lot in city or town or 20 acres in country. Personal property, specified items. 30 days' wages not exceeding $75 if necessary for support of family. When debt is for family expenses within last 6 months, 50% of wages not exempt.

**Pennsylvania** — Homestead, none. Personal property, $300; not limited to personalty, but may be allowed out of real estate. Wages, all.

**Rhode Island** — Homestead, none. Personal property, household furniture to $300, working tools, books to value $300, professional library and several other items. Wages, $10 exempt except as against debts for necessities; salary and wages of wife and minor children.

**South Carolina** — Homestead, $1000. Personal property, $500 to head of family; $300 to single man. Wages for 60 days, if family depends on them.

**South Dakota** — Homestead, 1 acre in town or city, 160 acres in country, value $5000. Personal property, $750 to heads of families; $300 and specified items to single persons not heads of families. Wages for 60 days if necessary to support of family.

**Tennessee** — Homestead, $1000. Personal property, specified items. Wages 90%, up to $40.

**Texas** — Homestead, $5000 lot in city and improvements or 200 acres and improvements in country. Personal property, specified items. Wages, all.

**Utah** — Homestead, $1500, also $500 wife, and $250 each child. Personal property, specified items not exceeding $1000. Wages, ½ wages for 30 days, $30 per month if wages be less than $2 per day.

**Vermont** — Homestead, $500. Personal property, specified items. Wages, $10.

**Virginia** — Homestead, $2000. Personal property, specified items. Wages, not exceeding $50 per month.

**Washington** — Homestead, $2000; homestead declaration necessary. Personal property, specified items; to householder $1000 in addition. Wages, current wages to the amount of $100, if family is dependent thereon, with certain exceptions.

**West Virginia** — Homestead, $1000. Personal property, specified articles. Wages, none.

**Wisconsin** — Homestead, ¼ acre in town or 40 acres in country, if less than $5000. Personal property, specified items. Wages, 3 months not exceeding $60 per month.

**Wyoming** — Homestead, $1500. Personal property, $800 to married man; $300 to single man; also wearing apparel. Wages, ½ of wages for 60 days if necessary for support of family.

# GLOSSARY

**Abandonment.** The relinquishing of salvage to the insurers with a view to claiming the full amount of insurance.

**Abatement.** Discount or reduction in price.

**Acceptance.** The agreement (usually written on the bill) by the drawee of a draft to comply with the request of the drawer.

**Accord and satisfaction.** The settlement of a dispute by an executed agreement between the parties whereby the aggrieved party takes something different from his claim.

**Acknowledgment.** The avowal of the genuineness of one's signature to a document.

**Acquittal.** A judicial discharge; a verdict of not guilty.

**Action.** A legal process or suit.

**Act of God.** An inevitable accident against which ordinary prudence could not guard.

**Adjudication.** A judicial decision or sentence.

**Administer.** To settle, as an administrator, the estate of a person dying without making a will.

**Administrator.** One appointed by a competent authority to settle the estate of a person who died without leaving a will.

**Advancement.** A payment made to a child by a parent to be considered as a part of his share of such parent's estate.

**Affidavit.** A statement or declaration sworn to before some one authorized to administer oaths.

**Affirm.** To make a solemn promise to tell the truth under the penalties of perjury.

**Alias.** A Latin word meaning otherwise.

**Alibi.** Elsewhere.

**Alien.** A foreigner who is not naturalized in the country of his residence.

**Alienate.** To transfer property, particularly real property.

**Alimony.** The allowance granted to a woman on a legal separation from her husband.

**A mensa et thoro.** From table and bed; a limited divorce.

**Appraise.** To set a price upon.

**Appurtenance.** Something belonging to another thing and which passes with it as an incident such as a right of way.

**Arbitration.** The trial of a cause in controversy by an unofficial person or persons chosen by the contestants.

**Arraign.** To call to answer to an indictment before a court.

**Assault.** An attempt to do corporal injury to another.

**Assign.** To make over to another.

**Assignee.** One to whom a right or property is made over.

**Assignor.** One who transfers an interest in property.

**Assigns.** Persons to whom property mentioned in a deed may be assigned.

**Attach.** To take by a writ of attachment.

**Attestation.** The act of witnesses in avowing the execution or signature to a deed or other document.

**Attorney in Fact.** An agent appointed by a power of attorney.

**Bail.** To release on security.

**Bailee.** One to whom the goods of another are delivered.

**Bailment.** The delivery of goods to another in trust for a certain purpose.

**Bailor.** One who delivers goods in trust.

**Bankrupt Law.** A law by which if an insolvent debtor assigns all his property to another to be used for the common benefit of his creditors he is forever discharged from further payment of his existing debts.

**Barter.** To traffic by an exchange of commodities.

**Battery.** The unlawful beating of another.

**Beneficiary.** One who receives an income from a fund or an estate.

**Betterment.** Improvements made on real estate.

**Bigamy.** The offense of contracting a second marriage while an undivorced husband or wife still lives.

**Bill.** A formal complaint or petition to a court of equity. A proposed law.

**Bill of Lading.** A written contract of a transportation company acknowledging the receipt of goods and undertaking to carry and deliver them to a certain place for a consideration.

**Bill of Sale.** A writing under seal conveying the title to personal property.

**Bona fide.** In good faith.

**Bond.** A writing under seal agreeing to pay a certain sum of money or perform a certain act.

**Burglary.** The crime of breaking open and entering the dwelling or place of business of another with intent to commit a felony.

**By-law.** A rule or law agreed upon by the members of a society or corporation for their action.

**Caveat.** A warning or caution; an instrument securing to an inventor exclusive rights to his invention before the patent is granted.

**Cestuy que trust.** The beneficiary in a trust.

**Chancery.** A court of equity.

**Charge.** To lay or impose a duty or obligation.

**Charter.** A written instrument executed by the sovereign power granting a special provilege or exemption.

**Chattel.** Any specie of personal property.

**Chattel Mortgage.** A mortgage on personal property.

**Chose in Action.** Any personal chattel of which one has not the possession but a right of action to reduce it to possession.

**Chose in Possession.** Personal property in possession.

**Civil Law.** The Roman law; the municipal law.

**Client.** One who employs an attorney.

**Collateral.** Side by side and not in a direct line.

**Collateral Security.** An obligation given to guarantee the performance of another contract.

**Common Law.** Those customs, rules and decisions that in consequence of long usage have now come to have the full force and effect of law.

**Concurrent.** Running side by side in point of time.

**Condition Precedent.** See page 53.

**Condition Subsequent.** See page 53.

**Consanguinity.** Relationship by blood or birth.

**Conservator.** A guardian.

**Consideration.** The motive; the legal inducement to enter into a contract.

**Contract.** An agreement between two or more competent persons based on a consideration to do or not to do some lawful thing.

**Copyright.** The exclusive right given an author to his production.

**Corporation.** An artificial person; a body of persons associated together by law and endowed with the power of acting for some purposes as a single individual.

**Coverture.** The legal condition of a woman during marriage.

**Curtesy.** The life estate a husband has in real property of his deceased wife when there has been a child born capable of inheriting the same.

**Covenant.** A mutual agreement in writing.

**Crime.** A violation of law, punishable by death, a fine, or imprisonment.

**Damages.** A money satisfaction for an injury.

**Declaration.** The plaintiff's cause of action in a suit, set forth in a legal and orderly manner.

**Decree.** The judgment or decision of a court of equity.

**Deed.** A writing, signed, sealed and delivered.

**De facto.** In fact; in reality.

**Default.** An omission to do that which ought to be done.

**Defendant.** The party against whom an actions brought.

**Demise.** The conveyance of real property.

**Demur.** To pause; to raise an objection.

**Deponent.** One who makes oath to a written statement.

**Devise.** To grant by will, mostly used of real estate.

**Devisability.** Want of the legal capacity to do a thing.

**Dishonor.** Refusal or neglect to accept or pay a draft.

**Distrain.** To seize the goods of a tenant for payment of rent.

**Domicile.** The habitation of a person.

**Dower.** The estate a widow has in the real estate her husband owned during marriage.

**Draft.** An order or request drawn by one party on another for a certain sum of money.

**Due Bill.** An acknowledgment of a debt in writing.

**Duress.** The state of compulsion in which a person is illegally influenced to incur a liability or release a claim.

**Earnest.** Part of the purchase price paid to evidence the ratification of a bargain.

**Easement.** A privilege, such as a right of way.

**Eminent Domain.** The right of a sovereign body to take private property for public use.

**Emblements.** Growing crops.

**Entailment.** The act of giving an estate and directing its future descent.

**Equity.** A system of jurisprudence supplemental to law.

**Equity of Redemption.** The estate still held by a mortgagor.

**Escheat.** The falling back or reverting of the title to lands on the death of the owner leaving no heirs.

**Escrow.** A deed or other written instrument delivered to a third person to be held till some certain contingency happens and then delivered to the grantee.

**Estate.** The quantity of interest a person has in property.

**Estop.** To bar or hinder by some rule of law.

**Execution.** That writ which empowers an officer to execute a judicial sentence; the signing, sealing and delivering of a deed.

**Executor.** One who is named in a will to execute its provisions.

**Ex post facto law.** A law which makes an act done before its passage a crime.

**Fee Simple.** An absolute estate of inheritance free from any conditions.

**Fee Tail.** An estate of inheritance descendible to a certain line of heirs.

**Felony.** A crime punishable by death or imprisonment.

**Feme Sole.** An unmarried woman.

**Foreclosure.** A legal proceeding which extinguishes a mortgagor's estate.

**Franchise.** A right or privilege.

**Freehold.** Any estate of inheritance or a life estate.

**Grant.** To convey by deed.

**Guarantor.** One who agrees to warrant the performance of some act by another.

**Guardian.** One named to have the care and custody of the person or property of one legally incapable of managing his own affairs.

**Heir.** One who inherits.

**Heirloom.** Any chattel which by law descends with land to the heir.

**Hereditament.** Anything which may be inherited.

**Incorporate.** To form into a corporation.

**Indorse.** To put one's name on the back of an instrument with intent to evidence a contract.

**Infant.** A person not of age.

**Injunction.** A writ issued by a court of equity prohibiting a person from doing a certain thing.

**Inquest.** A judicial inquiry.

**Intestate.** Dying without making a will.

**Joint Stock Company.** A partnership partaking of some of the features of a corporation.

**Joint Tenancy.** That peculiar method by which two or more persons hold real property in common, the share of one to go, on his death, to the survivor or survivors.

**Judgment.** Decision of a court.

**Jurisdiction.** The legal authority of a court.

**Law Merchant.** A system of rules deduced from the customs of merchants, by which trade and commerce are regulated.

**Lease.** The instrument by which an estate for years is conveyed.

**Legacy.** A gift of goods and chattels by will.

**Legal Tender.** That money which the law authorizes a debtor to offer in payment of a debt.

**Lien.** A right to retain another's property until a demand is satisfied; a charge upon real or personal property.

**Liquidated Damages.** That sum of money agreed upon in advance as damages in case of a breach of an agreement.

**Malfeasance.** A wrongful act.

**Mandamus.** A writ issued by a superior court to an inferior, or to an officer, commanding something to be done.

**Merger.** The absorption of one contract by another.

**Misdemeanor.** An offense punishable by a fine only.

**Mortgage.** A deed with a clause of defeasance; a pledge.

**Negotiability.** That property of certain contracts by virtue of which when they are transferred under certain conditions, they pass free and clear of defenses.

**Notary Public.** A public officer before whom acknowledgments of deeds, oaths, etc., may be taken.

**Ordinance.** A law of a minor municipal corporation.

**Parol.** By word of mouth.

**Parol Contract.** Any contract not under seal.

**Plea.** The formal allegation of fact which a defendant makes to the plaintiff's declaration.

**Pledge.** Anything deposited as security.

**Politic.** Promoting good policy.

**Posthumous.** Born after the death of the father.

**Post mortem.** Made after death.

**Power of Attorney.** The sealed instrument by which one appoints another to act in a given matter for him.

**Presumption.** An inference of law from certain facts.

**Primogeniture.** The right of the eldest son to inherit his ancestor's estate to the exclusion of younger sons.

**Probate.** To prove; to prove a will.

**Property.** The exclusive right one has to anything.

**Protest.** An act by a notary done for want of payment of a note or draft or the acceptance of a draft.

**Proxy.** A substitute.

**Quantum meruit.** So much as it deserves.

**Quantum valebat.** So much as it is worth.

**Quasi.** As though.

**Quo Warranto.** By what right.

**Real Estate.** Property consisting of lands and all that is permanently attached thereto.

**Realty.** Real estate.

**Recognizance.** A bond.

**Recoup.** To keep back part as a claim for damages.

**Release.** A relinquishment of some right; a quit claim deed.

**Remainder.** An estate to take effect after another's estate is determined.

**Replevin.** An action to recover the possession of goods wrongfully taken and detained.

**Residuary Devisee.** The person named in a will to have the balance or remainder after all other devisees are paid.

**Salvage.** A compensation for saving a vessel from wreck.

**Scilicit.** To-wit; namely; abbreviated in legal documents to *ss.*

**Sentence.** The judgment of the court in a criminal case.

**Specialty.** A contract under seal.

**Specific Performance.** An action in a court of equity to compel a party to perform his contract in precise terms.

**Statute.** A law made by the legislature.

**Subpoena.** A writ commanding the attendance of a person in court under penalty.

**Subrogation.** The substitution of another as a creditor.

**Summon.** To give notice.

**Tenant.** One who has the temporary possession of the lands of another.

**Tender.** An offer of a chattel or money in satisfaction of a debt.

**Tenure.** The mode by which one holds an estate in lands.

**Testament.** A will.

**Testator.** One who dies leaving a will.

**Tort.** A wrongful act for which an action will lie.

**Trust Deed.** A deed conveying real estate to another to be held in trust for the benefit of a third person.

**Unilateral.** One sided.

**Usury.** Illegal interest.

**Vendor.** A seller.

**Verdict.** The decision of a jury reported to the court.

**Vested.** Fixed; already in force; not liable to be set aside by a contingency.

**Waive.** To relinquish.

**Warrant.** To guarantee.

**Waste.** The destruction done or permitted to houses or woods of an estate by the tenant thereof.

**Will.** An instrument by which a person disposes of his property to take effect after his death.

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